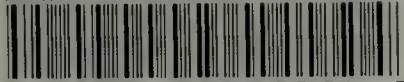


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**BRIEFING ON U.S.  
ASSISTANCE TO CENTRAL  
AND EASTERN EUROPE  
AND THE NIS: AN  
ASSESSMENT**



February 17, 1995

Briefing of the  
Commission on Security and Cooperation in Europe  
Washington, DC



# BRIEFING ON U.S. ASSISTANCE TO CENTRAL AND EASTERN EUROPE AND THE NIS: AN ASSESSMENT

Friday, February 17, 1995

Commission on Security and Cooperation in Europe,

Washington, DC.

The Commission met at 10 a.m., in room 2200, Rayburn House Office Building, Washington, DC, David M. Evans, moderator, presiding.

Present: David M. Evans, Thomas Dine, Serge Duss, Linas Kojelis, and John D. Sullivan.

Mr. **Evans.** On behalf of the Commission on Security and Cooperation in Europe I would like to welcome you this morning to this briefing on "U.S. Assistance to East-Central Europe and the NIS; An Assessment." My name is David Evans. I am the senior advisor to the Commission, and I will be your moderator this morning.

As many of you, perhaps most of you, probably know, the Commission, commonly called the Helsinki Commission, was established in 1976 by the Congress to monitor and encourage the implementation of the Helsinki Final Act and subsequent accords of the CSCE, which is now the OSCE, the Organization on Security and Cooperation in Europe.

The Chairman of the Commission is Representative Chris Smith, and the Co-chairman is Senator Alfonse D'Amato. The Commission is composed of 9 Senators, 9 Representatives, and 3 members from the executive branch, a representative each from the Departments of State, Defense, and Commerce, for a total of 21 Commissioners.

The Commission has a wide range of activities, including congressional hearings, congressional trips to areas of concern, participation in the many activities, meetings, and so forth of the OSCE itself, including the OSCE parliamentary assembly, and just recently last year we began this format of briefings which we have found to be very effective to focus on particular interests and particular areas of concern.

Much of the Commission's focus over the years has been in the area of human rights, as well as regional security, but the third major area and component of the OSCE is, as you know probably, the economic area and assistance. Assistance to the New Independent States and emerging democracies in the region has been of great interest and concern to the Commission for the last couple of years.

This year, particularly, with the developments in Chechnya, we thought it appropriate to hold such a briefing this morning. We have set for ourselves an ambitious agenda. Discussion of U.S. assistance to Central and Eastern Europe and the countries

of the former Soviet Union for geographic reasons alone could easily have been the subject of several briefings.

In addition, within the region the pace of democratic reform and transition to free market economic systems has varied widely from country to country, creating a multi-tiered effect on the transition.

Both the successes achieved and the difficulties encountered on the road to democratic reform and stabilization are reflected throughout the region and have had an impact on the scope and tenor of U.S. assistance programs. Since 1990, U.S. assistance to East-Central Europe and the NIS, including food and nuclear weapons reduction programs, exceeds \$9 billion. These programs involve assistance to countries throughout the region in democratic institution building, market reform and restructuring, health care improvement, energy efficiency, environmental policy, and housing sector reform.

The President is asking for \$1.4 billion in assistance for the region in fiscal year 1996. Many see this type of assistance as critical to United States security and economic interests in the region. However, some observers have criticized United States efforts as slow to materialize, uncoordinated, too Russia-centered, and lacking evident positive results at the grassroots level.

Regardless of one's views on specific programs, it appears certain that the crisis in Chechnya, continued conflict in the Balkans, and tensions in various parts of East-Central Europe make successful reform in the region even more important to United States interests today.

The Congress will, in the coming months, be reviewing and scrutinizing all funding for the region. This morning we will focus on the goals of U.S. assistance to the NIS and East-Central Europe and the effectiveness of current programs in furthering those goals.

We are very pleased to have with us a distinguished panel of experts to address these issues. Mr. Thomas Dine, to my right, is Assistant Administrator of the U.S. Agency for International Development, USAID for Europe and the New Independent States. A foreign and defense policy expert, Mr. Dine has worked during his career in national security affairs for the U.S. Government and a think tank and academic institutions.

Before joining USAID, he headed the American-Israel Public Affairs Committee, AIPAC, from 1980 to 1993. Prior to that Mr. Dine worked in the U.S. Senate for 10 years, serving as national security staff director of the Senate Budget Committee, legislative assistant for foreign affairs to the late Senator Frank Church, SALT advisor to former Senator Edmund Muskie, and deputy foreign policy advisor to Senator Kennedy.

Mr. Serge Duss, to my far right, is Associate Director for Government Affairs of World Vision, an international relief and development organization with programs in more than 95 countries. Resident in Moscow from 1991 to 1994, he served as field director for development projects, focused primarily on training and education, which were initiated in five republics of the former Soviet Union.

Before coming to World Vision, Mr. Duss directed Soviet and Indo-Chinese refugee programs with World Relief in the 1980's. He also served as a program officer for refugee affairs at Interaction, an association of American private voluntary organizations involved in international projects.

Mr. Linas Kojelis, to my left, is here today representing the Central and East European Coalition, an organization composed of 16 national membership organizations. As



president of the U.S.-Baltic Foundation, Mr. Kojelis has implemented programs in the region involving local government, rule of law, and public health.

Prior to joining the U.S.-Baltic Foundation, Mr. Kojelis served as Deputy Assistant Secretary of State for Refugee Admissions and, in the White House, as Special Assistant to the President for Public Liaison.

Dr. John Sullivan, to my far left, is executive director of the Center for International Private Enterprise, CIPE. An affiliate of the U.S. Chamber of Commerce, CIPE is mandated to advance private enterprise and market institutions that support democratic development. Under Dr. Sullivan's leadership, CIPE has provided financial support and technical assistance for 250 projects in over 45 countries.

Dr. Sullivan joined CIPE in 1984, a year after its inception. Prior to that, he served for 2 years as director of the Washington office of the International Center for Economic Growth, and before that he was associate director of the Democracy Program and director of Business and Economic Education for the U.S. Chamber of Commerce.

Our format this morning will be that all four presenters will speak, and then following that we will open up to questions and answers.

Mr. Dine, will you please lead off?

Mr. **Dine**. Thank you very much, David.

The first thing I would like to say is what I observe. It has been a long time since I have seen a roomful of people in Washington concerned with American foreign policy, and American foreign assistance programs. In a period of focus on domestic policy and programs, I am delighted to see a standing room only crowd.

I am here to talk about the work of the U.S. Government, in particular about the U.S. Agency for International Development's efforts to develop the private sector in the Central and Eastern European countries, as well as in the former Soviet Union countries.

Basically 80 percent of American appropriated funds for this area of the world goes to the goal of helping to create a private sector. This is an integrated program, and I think it's one that is in the interest of the United States.

All of the former Soviet Bloc countries, 27 of them, are in transition. They are going from totalitarianism and one-party power to nascent democracy and political pluralism; from central planning, military production, and plant quotas to competitive market economies; from closed societies where knowledge was secret to open societies where information about human tragedy in Chechnya or corruption in Prague or the failure of economic growth in Tajikistan is now revealed to the public; from isolation in an internationally stagnant bloc to the beginnings of integration into the global community. So this is a profound, a profound transition.

Stated most directly, America's goal, the U.S. Government's goal, our challenge in the entire region, is to help create an environment for prosperity. If you look back historically to the Marshall Plan, 1948 to 1960, when appropriated moneys were provided to that effort, we tried to help Western Europe reconstruct and recover, and we did. The United States Agency for International Development today is trying to help the countries of the crumbled Soviet empire to restructure themselves one by one as democratic, free market oriented commonwealths, and hopefully these countries will then join the broader commonwealth of free nations.

For the peoples of the whole area to restructure and rebuild, all of this means a 180 degree turn. It means, first, undoing the failed Soviet legacy, and you still see this effort today everywhere one goes.

Second, it means a long-term transformation, psychological, material, political.

It is in the U.S. national interest that radical political and economic change take place. It is in the U.S. national interest that this change be irreversible. All of this is in the vital interest, I believe, of the Central and Eastern European countries and the former Soviet Union countries as well.

The transition to business friendly societies is a win-win situation if we can achieve it.

Let me stress three thrusts of the U.S. Government's efforts, especially USAID's, in trying to achieve our national objectives. First is targeting reformers in reforming countries. A simple sentence, a clearcut goal, a clearcut strategy. We are directly linked to the change agents in each of the countries.

Last week I participated in a fact finding delegation that went to Ukraine, Belarus, Georgia, and Armenia to size up the reformers in these newly emerging reform countries. We believe that these four countries are the next wave, the second wave, if you will, of reform, and it is important from the perspective of our national interest that we be engaged with this effort.

The first wave in the former Soviet Union was led by Russia. Russia today is way ahead of the rest of the countries. But Moldova, Belarus, and Kazakhstan have also been reforming, and we are engaged with their reform leaderships.

In the Central and Eastern European area, reform came quickly after the Berlin Wall came down in 1989. Reform came quickly to Estonia, Latvia, Lithuania, the four northern tier countries of Poland, Hungary, the Czech Republic, and Slovakia, and is coming much slower in the southern tier countries, Romania being ahead of Albania and Bulgaria, and as our moderator said, we have got problems in the Balkans where they are engaged in war, not reform.

So the first thrust is to be on the side of the reformers; engage with the reformers as they go about being the change agents in their own societies.

The second key thrust is private entrepreneurship, the driving force, the turbo engine, if you will, that will create and sustain market reform. Privatization is the foundation of this change. It is the critical element in the overall transformation process.

Most of U.S. foreign assistance to this part of the world is directed to mass privatization, post-privatization, economic restructuring, as well as democratic reform which is, I believe, entwined with the whole economic change.

The leaders clearly are Estonia and the Czech Republic, which has had a dynamic, clear sighted, forceful leadership in its Prime Minister. Poland, which has had three straight years of real growth and last year reached 4 percent. Perhaps this year Poland will have up to 7, 7½ percent growth. Russia has had its problems, certainly articulated in the press every day and in every way. Russia by the end of June 1994 had concluded the biggest sell-off of state property the world has ever witnessed in just a short year and a half period of time.

The privatization program has resulted in quite literally the dismantling of communism, the undoing of state ownership of the means of production, the end of the command economy. Vestiges, however, still remain. I have vividly in my mind as I say those

words being in Belarus last week. It is the only country that I know of that wants to belong to Russia again, to be part of a command structure somehow or other again, Russia's leadership has rejected that desire to come back.

In Russia, more than 70 percent of the country's productive property, comprising 20,000 large enterprises and about 100,000 small businesses, is now in private hands. Sixty-five percent of the Czech Republic's GDP is due to a private sector. Over 55 percent at least in Estonia and Latvia, probably Lithuania as well, 55 percent of the GDP is now due to the private sector, and 50 percent we estimate of the GDP of Russia is the private sector, both official and unofficial.

And I would make a prediction here that a year from now if we sit, we will be able to say something similar about Ukraine because I believe under President Kuchma that country, that rich country, now has direction, and its government is assembled around that direction, and I believe the reform, that long awaited reform in that very important and rich country will take place.

The third key thrust of USAID is the promotion of wholesale structural change, structural changes in the political, economic, and social systems. In our projects we are linking politics and law, on the one hand, and economics and business on the other. A business friendly environment depends upon the rule of law, upon well ordered institutional and regulatory framework, upon the predictability, transparency, and enforceability of norms of commercial conduct.

For the next few years, USAID, the Treasury Department, and USIA, the Energy Department, a whole host of agencies, even the New York Federal Reserve Bank, will be engaged with the moneys that Congress authorizes and appropriates to fulfill these goals.

I mention the New York Federal Reserve Bank because Viktor Yuzhchenko, National Bank Chairman of Ukraine, is in town this week. We are doing projects with him, with his central bank, through the New York Fed. This gives you an idea of the vast array of resources America has, the kinds of technical assistance knowhow that gets transferred abroad, and in ways that I think achieve what we are all after.

USAID is developing capital markets, establishing equity and commodity exchanges, and other trading infrastructure. We are about establishing responsible regulatory agencies, for instance, analogues to our Securities and Exchange Commission, as well as practices of commercial self-regulation, such as we have on the New York Stock Exchange and the NASDAQ.

We are instituting modern financial accounting standards throughout these countries in their various financial, budgetary, economic structures. We are developing rules and standards of corporate governance dealing with these newly privatized entities to try to make them work. We are drafting, helping draft modern commercial laws.

I might note that on January 1, 1995, the first part of the new Russian civil code containing many of the basic commercial laws went into effect.

And we are overhauling irrational taxation systems to establish a clear, fiscally sound, and nonpunitive tax regime. We are also perhaps bucking our heads against the wall in certain countries trying to privatize land, but we are trying to bring land reform to all of these countries in a modern business sense.

And finally, we are deeply engaged with all of these countries outside of their capital cities. You cannot do one without the other. I myself from my Peace Corps background and the organizing I did for 13 years at AIPAC believe in the bottom-up. I also know in

this kind of setting where we are trying to change structures 180 degrees, you must also go from the top down. That is where the new laws must come from, the new national institutions and structures.

We are supporting reformers then to achieve structural change, trying to build a constituency for the change, helping to open up the diverse new business opportunities to the world market, and I hope we play an effective role throughout this decade and then get out, exit.

Before the century ends, I believe the results in Central and Eastern Europe, as well as in the New Independent States of the former Soviet Union will match, if not exceed, the results of the Marshall Plan. If I am right, the West will have won not only the cold war, but more importantly, the peace that followed.

Thank you.

Mr. **Evans.** Thank you very much.

I think we will now turn to Mr. Duss. Serge, would you please?

Mr. **Duss.** Thank you, Mr. Chairman, for the opportunity to contribute these brief comments as we try to assess United States assistance to Central and Eastern Europe and the New Independent States of the former Soviet Union.

Since my specific area of expertise is the New Independent States, I will enter my comments on that geographic area and focus more on the perspective from one active in the grassroots level.

Living and working in Russia for almost 3 years, arriving in Moscow only weeks after the attempted coup against President Mikhail Gorbachev in 1991, allowed me to witness an event several months later very few thought would take place in this century: the termination of the Soviet Union as a political state.

However, the question of dissolving the Soviet welfare state culture molded over 70 years and three generations and whether it evolved into a civil society where a free market flourishes is quite another issue.

At the start the U.S. assistance program to the NIS, particularly Russia, was well intentioned with its emphasis on promoting a market economy and fostering an emerging civil society. However, United States rush to demonstrate support for and solidarity with the new fledgling Russian Government resulted in two major problems which dog the program to this day.

First, Russian reformers and reform institutions were simply unable to responsibly absorb the aid, more than \$1 billion in fiscal year 1994. It did not have the legal and civil infrastructure to accommodate privatization for the most part.

Even though companies may be privatized on paper, they are still controlled by Soviet era directors and operate along the principles of a command economy that are resistant to change.

Small businesses, the key to any thriving free market economy, appear to have missed out on a substantial amount of foreign aid. A recent poll conducted by the Center for Economic Reform in Moscow reveal that only .3 of 1 percent of the small businesses surveyed across Russia, just five out of 1,628, had managed through the help of professional associations to get any international assistance.

In addition, I think too much emphasis was placed on short-term results, jump starting the economy rather than long term. Believe me; nothing is ever jump started in the former Soviet Union.

No. 2, USAID money was dispersed to agencies and contractors that were simply ill prepared to achieve the objectives of the assistance program. One pool of well prepared groups that could have been utilized for project implementation in the NIS, particularly in Ukraine and the Baltics were American ethnic organizations. These organizations are comprised of professionals who speak the language fluently and, more importantly, understand the culture and are committed to the long term.

In addition, before the Bureau for Eastern Europe and the NIS was created at USAID, layers of bureaucracy were actively involved in the decisionmaking process for grant approval.

It's my observation that U.S. assistance programs that focus on the grassroots, the common folks who make up the vast majority of the countries, derive the greatest payback on it investment. Programs that sought to build and strengthen civil society through the development of a variety of citizen voluntary organizations, including self-help associations, empowered those in post-Soviet society who had never before had the right to govern their own destinies:

Programs that focus on management training, education about democracy, rule of law, and free markets inspire and empower formerly powerless people to think for themselves and begin to resolve their own problems utilizing their own available resources.

As the U.S. Government funding begins to decrease in the NIS, programs should begin to focus more on developing a democratic infrastructure, strengthening civil society by training and educating present and potential leaders in these communities. What we must understand is that a social revolution is just beginning to take place in Russia, the Baltic Republics, and Armenia, and less so in the other NIS republics.

This social revolution supersedes political and economic changes. Communities and individuals conditioned to subservience to the state are for the first time dealing with choices and for many it is a very scary experience.

We should also understand that United States assistance, in fact, all Western assistance to the NIS but especially to Russia, is merely a stimulant for a free market development and civil society. Therefore, the U.S. should use diminishing resources to till and cultivate the grassroots so that whatever seeds of aid are invested will be nourished by communities prepared to develop and promote trust, fairness, cooperation, tolerance, and inclusion.

I would suggest that during the remaining years of the U.S. assistance program it focus more on smaller scale privatization, the shopkeepers of the NIS, and target sectors of society that will impact the greatest number of people.

Some suggestions: one, help rebuild educational systems. Schools are starving for new textbooks and curricula free of communist ideology. Funds should be redirected to create books, videos, and films that explain democracy, free markets, political, ethnic, and religious pluralism.

Enthusiastically support legal reforms. Legal systems in all the republics continue to reflect the arbitrary nature of Soviet justice. Legal reform programs should be strengthened. Support must be provided for building an adequate court structure and creating legal associations.

Significantly increase the number of exchange programs for NIS students and budding community, political, and business leaders, and let's not be shy about incorporating the study of ethnics and the vital role of moral values in civil democratic society.

In Russian there is a single word that characterizes all of the envy, hate, and tired mediocrity of the Soviet legacy. The word is "sovok." It's a slang term derived from "sovyet," as in "Sovyetskiy Soyuz," the Soviet Union.

A 1992 article in one of Russia's first independent newspapers, *Nezavisimaya Gazeta*, describe the "sovok" as a person with a crazed thirst for equality, a deep hatred for the success of others, and a flourishing laziness.

Ultimately it's the "sovok" mentality that stands as the greatest obstacle to political and economic reform and the steady emergence of civil society and democratic institutions. Only as United States assistance programs in business, government, and social sectors are able to help citizens of post-Soviet republics shed the "sovok" mentality can we have any real hope of success in the NIS and achieving the program's goals for the benefit of future generations.

Thank you.

Mr. **Evans**. Thank you very, much, Serge.

Next we will turn to Mr. Kojelis. Linas, you have the floor.

Mr. **Kojelis**. Thank you.

I am pleased to speak on behalf of the Central and East European Coalition on U.S. Government assistance to Central and Eastern Europe and the New Independent States of the former Soviet Union. We are especially pleased to speak before this Commission because it is this Commission, the Helsinki Commission, which for decades has focused and studied the fundamental issues which should be at the heart of U.S. assistance to the region: human rights, democracy, and free markets.

The U.S. assistance program of the past 5 years and the foreseeable future should have been a dream come true for that cluster of individuals and organizations which we can call the Democracy-Human Rights Community. This is the community which worked side by side with this Commission, organizations like Helsinki Watch, Amnesty International, Freedom House, and a host of others, in the long, hard struggle against totalitarianism in Central and Eastern Europe and the former Soviet Union.

All of the members of the Coalition I represent this morning are charter members and veterans of the Democracy-Human Rights Community. We, like you, know fully and understand deeply the wholesale harm done to the countries of CEE and NIS by communism and the excruciating pain and difficulty of the current democratic transformations.

We have worked side by side with you for the past two decades and will continue to work with you far into the future. For organizations like ours, the waste, fraud, and abuse which have become the hallmark of United States assistance to Central and Eastern Europe and the New Independent States is ironic and painful. Everyone in the Democracy-Human Rights Community understood the joy of learning that another hand typed issue of a "samizdat" publication had been successfully smuggled to the West or the anguish in hoping that a letter or a package to a prisoner of conscience in the Gulag might actually be received by the addressee.

In those hard and dark years, there were no fat U.S. Government contracts to promote democracy, human rights, and free markets in the region. We did it all dissident by dissident, dollar by dollar.

I will not try to recount the never ending list of criticisms U.S. assistance programs chronicled regularly by the media. Anyone with access to an on-line media data base simply needs to key in the phrases, "U.S. assistance", "Central and Eastern Europe", "former Soviet Union", and "waste", and can then harvest a bounty of articles, reports, and studies documenting the problem.

We are including as an addendum to this testimony four such articles from the Wall Street Journal, U.S. News and World Report, and the Washington Post. The squandering of hundreds of millions of dollars of precious democracy and human rights development funds is beyond words.

What exactly has gone wrong with the process, and what can we do to change it?

The problem began at the very start. The moment Congress appropriated the first substantial funds, called seed and freedom assistance funds, the management of these funds was overseen not by the veterans of the Democracy and Human Rights Community, but by government technicians and bean counters and a host of generic international development, fee for service contractors almost none of whom had the least bit experience in the fight for freedom in Central and Eastern Europe and the New Independent States. The Democracy-Human Rights Community was not even consulted in the design of these programs.

The disenfranchisement of this community of dedicated and knowledgeable experts in the design and management of U.S. assistance programs for the countries of CEE/NIS is without question the most fundamental reason for the tragic waste of hundreds of millions of dollars over the past 5 years.

Consequently, integration of the Democracy-Human Rights Community and to all current and future programs should be a top priority of this Commission and this Congress.

A second vital issue is the contracting process of U.S. assistance agencies, especially USAID. Issues related to this process are extremely byzantine and cumbersome. However, they are critically important to the purpose and success of U.S. assistance to this region.

To date Congress has shown much greater interest in the total sums of dollars appropriated for the region than for the processes by which this money is actually transformed into concrete assistance, which is often not appropriate to nor meets the needs of target countries.

Our friends on congressional staffs admit that their eyes glaze over when we begin explaining the technical details of RFPs, RFAs, IQCs, and all the other alphabet soup. Others have even berated us for wasting their time with such matters.

But the bottom line is that the failure of Congress to focus on the details of the contracting process guarantees the continued mismanagement of a huge proportion of these funds.

Our Coalition prepared a 15-point plan last year to begin the reform of this arcane and wasteful process. These reforms include ending CEE or NIS region-wide contracting processes, which fail to reflect the specific needs of individual countries; requirements that contractors have specialized knowledge in the region; requiring that U.S. Government program designers use knowledgeable experts in the design of programs; requirement that

contractors have a long-term commitment to the region that will transcend the U.S. Government-funded work.

Routine public disclosure of specific tasks, goals, and funding levels of USAID contracts, insuring an open and fair process for awarding grants and contracts, and streamlining and simplifying the contracting process to encourage entry by smaller region specific organizations are also called for.

These are common sense solutions, and our Coalition is wholly bewildered by the vociferous opposition by the administration to these simple reforms.

Without question, the one provision the opponents of AID contracting reform fear most is the requirement that contractors have a long-term commitment to the region. Quite simply, this requirement would eliminate over 90 percent of the contenders for these scarce funds.

This requirement goes directly to the question of which organizations and individuals have a solid track record which proves that they know and that they care about the fundamental issues involved in the reform of post-communist societies. Are they the gaggle of beltway bandits or generic international service PRO's which endlessly search the pages of Commerce Business Daily for the next fat Federal contract to come along, or are they the ones that have been hard working partners of this Commission for the past two decades and which will continue this commitment to strengthen human rights, democracy, and free markets long after the last USAID office shuts down in Central and Eastern Europe and the former Soviet Union?

It is no accident that right now a debate rages in Congress about returning control of local programs to local governments because running them from Washington has simply not worked. This is our recommendation exactly. Use region specific organizations, including many in our ethnic communities, in the assessment and delivery of U.S. assistance.

Why? Because we know the area, the language, the people, and the pitfalls; because we represent the range of American private sector interests, business, humanitarian, religious, social, cultural, and others who are investing tens and soon hundreds of millions of private sector dollars, in kind donations, and volunteer services into this region because we are not there for the short haul or the fast profit.

We and our children are going to visit, in some cases live, and experience first hand the consequences of these assistance programs, and we want to see them succeed because we can serve as a permanent bridge between the United States and those countries.

But the issue is not just increased effectiveness and efficiency in our foreign assistance programs. There's an even more important reason for immediately engaging both U.S. Government departments and agencies and private sector organizations with long-term interests in the region. What is at stake here? Nothing less than the National security interest of the United States.

In this century the United States was called upon to fight two World Wars and 45 years of a cold war, conflicts which emanated from the heart of Europe in the furtherance of vital U.S. geopolitical interests. There is no greater United States interest than the dismantlement of the Soviet Warsaw Pact strategic and conventional threat to the United States and our European allies.

The institutionalization of democracy and market economies and respect for human rights in Central and Eastern Europe is the best means of guaranteeing that there will



be no return to the days of the cold war nor any future European conflicts which will entangle the United States.

The achievement of that objective, however, requires the continued long-term engagement, support, and assistance of the United States and the West.

An investment in peace, stability, and democracy in Central and Eastern Europe serves U.S. long-term interests in other ways. After investing tens of billions of dollars in the cold war, that investment now required to effectively run the United States assistance programs in the region pales by comparison. The investment in democracy building today will pay dividends through a long-term security and reduced military expenditures for the United States.

In assuming the management of U.S. assistance to the region, USAID and its contractors unambiguously proclaim that they will be in Central and Eastern Europe only for the short run. From the very start these agencies and their congressional supports have promoted a shutdown schedule with which they will "graduate" individual countries from U.S. assistance as quickly as possible.

To date AID has failed to provide a rigorous, comparative, objective analysis and explanation for its graduation timetable and standards, an issue worthy of separate hearings. This approach is incompatible with U.S. long-term strategic interests in the region.

The end of communism and CEE/NIS and the tearing down of the Berlin Wall have opened up a whole new era for American foreign relations for both the public and private sectors. As President Clinton said in Berlin last year, everything is possible.

Many of these new opportunities are exciting and wonderful. American businessmen are exploring all sorts of promising new investment and trade opportunities. Families and friends are meeting again for the first time after half a century. Colleges and museums are exploring and finding whole new worlds of science and long lost worlds of culture.

Other conditions are tragic. The environmental community is groping with catastrophes it could never have imagined. Grassroots democracy building in the area of public administration cries out for assistance. Human rights and welfare organizations are just beginning to comprehend the human devastation of decades of intolerance and inhumanity.

Whether it is building on new opportunities or trying to solve the human or environmental disasters, U.S. public and private agencies have long-term strategic interests in the region. In this context, the bottom line turns out to actually be very simple. The United States has long-term strategic interests and needs in the region. Thus, it is vitally important that all short-term U.S. assistance programs be designed and implemented in such a fashion as to further those strategic interests and needs.

The issue before this Commission, before this Congress, and before the entire country is not fiscal year 1996 funding levels for CEE/NIS. The issue is: what should U.S. relations with that region look like 15 and 30 years from now, and what must we do today to make this happen?

The current process of managing U.S. assistance to the region is fatally incompatible to this goal. A U.S. agency with an emphatic, short-term interest in the region is managing billions of dollars which will form the bedrock of long-term U.S. relations with these countries well into the next century. This is a guaranteed formula for continuing catastrophe.

Thus, we ask the Commission to fully engage in the zero-based analysis of management of U.S. assistance. We welcome the efforts of the Secretary of State, the Chairman of the Senate Foreign Relations Committee, and others to wholly reinvent the foreign assistance bureaucracy. Our concern, however, focuses less on the organizational structure of that bureaucracy and more on the delivery of effective and efficient assistance to the Nations of Central and Eastern Europe.

The recommendations of the Coalition provided in the addendum to this testimony could serve as the basis of any reform effort. The reinvention will be judged by its results.

In summation, we urge the Commission to focus for the short term on immediate remedies the coalition has recommended for USAID and other agency contracting processes, all of which can be implemented administratively with no new legislation. For the long run, we ask that the Commission and the relevant authorizing and appropriating committees consult closely with members of our coalition in the process of reinventing foreign assistance.

We thank you for allowing us to be with you this morning, and we will be happy to answer questions.

**Mr. Evans.** Thank you very much, Linas, for that very forceful statement.

And now, Dr. Sullivan, you have the floor.

**Dr. Sullivan.** Thank you very much, Mr. Chairman.

Well, one of the problems with being the last speaker on a panel like this is that you're tempted to try to escalate one level further, but I think I'll declare at the outset that is not possible. Those were very interesting presentations.

The work of our Center for International Private Enterprise or CIPE, as we call it, is based on the experience of our parent organization, the U.S. Chamber of Commerce. As many of you may know, the Chamber formed CIPE as a separate affiliate in order to be involved with the National Endowment for Democracy originally, and now we have received as well some limited USAID funds for Hungary, the Baltics, and a few other countries in Central Europe exclusively. So I am going to be talking today about that experience base.

Our experience through the Chamber, of course, goes back over 30 years in the Central and Eastern European region because we have had bilateral business councils or bilateral economic councils, more precisely, since they did not have what you would recognize as private enterprise in Central Europe for most of that time.

That experience that we had at the Chamber both gave us a base to begin our programs from, as well as pointed up the difficulties that we thought would be expected through the transition process. The experience was not always a happy one between private business members of our councils and their counterpart groups who tended to be the official Chambers of Commerce.

We were trying to push for reform, trying to push for market opening measures, trying to push for a variety of other things, and they were mainly trying to create or craft special kinds of operations where they could entice investors into their countries. So there was always a dynamic tension.

That has changed considerably, and what I thought would be useful to comment on today is to really talk about the strategy that we have adopted at CIPE and to draw on a portfolio of projects, some 60 projects, that we have been involved with throughout these two regions.

I am not going to go into detail about the types of projects. On the table over here we have provided a portfolio, little descriptions which combine the experience base of many of these programs.

Let me just say that for the most part what we are involved in are partnerships, as we look at it, with private indigenous groups, usually associations of private entrepreneurs, sometimes foundations, or public policy research institutes that have started and that are now private. They have either started new or they have been transitioned out of the state sector, only rarely are the Chambers of Commerce partners for our programs.

As you may gather from what I said a moment ago, to this day the Chambers in most of the countries in this region still are official structures. They are either overtly official or they are covertly official. Poland is one exception, and there are a few others that are now beginning a transition process.

Let me do add one caveat though to what I am saying here, and that is that although the purpose of today's hearing, for which I congratulate the Commission, is to focus on the broad array of U.S. assistance programs, what I am talking about really is what might be known as the grassroots projects. The kinds of things that our other two panelists have talked about. The lessons that I am going to draw out of that one would have to take somewhat of a leap, and I think it has to be taken cautiously, to apply them to the other types of assistance programs where you are in a government-to-government mode, which is much more difficult in my view.

By way of background, I would agree with a lot of what has been said about the progress in the region. We also have here a magazine that we publish called Economic Reform Today. The current issue of that magazine contains statements by indigenous research centers for many of the countries in the region, and I welcome you to take it.

We also have detailed background papers that these same organizations, groups like the Gdansk Institute in Poland or the Lithuanian Free Market Research Institute in Lithuania. These are their views and what they see in terms of progress.

And as might be guessed, it is basically a much brighter picture in Poland, Hungary, the Czech Republic, the Baltics, at least in Estonia and Latvia; somewhat less optimistic picture in the southern tier countries, and I'm excluding the war zone here. Progress is much slower in that region.

In our view, we do not have a statement in here from any of the Russian or Ukrainian groups, but in our view the progress in those regions is much less.

One thing I want to point out about this material though. First, it is difficult, I think, even in a group like this to be able to treat this issue of how much progress has been made objectively and fairly. We have not established any benchmark or yardstick or accepted standards of any sort to be able to say what kind of progress should be expected, either directly from assistance or across the board in terms of the speed of transition, from a formal economics or scientific point of view.

The second point that could be kept in mind is that although there are not any accepted standards, there are some indicators. One of those indicators which has been alluded to most directly by Mr. Kojelis is foreign direct investment, and if one uses that as a measure, and since I am from the business community it has a certain appeal obviously; if you look at that as a measure, then you can say that it ratifies what I have just

said. The northern tier countries are where the action is. It is where people see the most progress, the most opportunity.

There are still problems. There are still uncertainties. There is still a much higher risk premium in these northern tier countries than you would find in any other kind of investment opportunity. Nevertheless, there is something happening there. It is beginning to pick up now in the southern tier countries for the most part, again excluding the war zones, but there is still enormous skepticism about Russia, about the NIS in general. Belarus is hardly on the radar screen. In the NIS people are looking at commodity based activities or extractive industries—that is you have to go where the oil is, you have to go where the aluminum is.

One other indicator, if you like, that captures this direct investment kind of phenomenon is that we have seen a remarkable transition from these U.S. economic business councils to the formation of American Chambers in each country. These Chambers, of course, are independent. They are members of our group. They are serviced by us, but they are independently incorporated, usually including a substantial number of national firms, over all the American Chambers must be predominantly American in terms of investment, not necessarily in terms of citizenship of the employees.

And we now have American Chambers in every one of the countries in Central Europe. In the southern tier, Bulgaria and Romania are coming on line. Bulgaria has formed one, and they are in the process of getting accreditation with the U.S. Chamber. Ukraine even has one.

Russia, however, has only just formed theirs, and they are not yet fully accepted, but I expect that they will be soon.

The fact that there are enough on-the-ground, American companies who want to be visibly known, who have come together through these Chamber structures, is another indicator of where the progress is.

I would agree with the points that have been made about the United States national interests. I mean historically put, the old issue of military security has changed fundamentally. These two regions' integration into the world trading system has raised a whole host of issues of importance to the United States, many of which in our view have not been fully addressed, including the flow of funds, the flow of investment dollars from the United States, in particular; disruptions in the flow of commodities that happen as a part of this process of transition, aluminum and oil being two classic examples.

I think we also though need to recognize at least one major success that has taken place in Central and Eastern Europe, and I am not referring to the NIS at this point. In our view democracy and market economics have become generally accepted as the preferred way of organizing society, and I think that is at least absolutely true at the level of the opinion leaders and emerging private sectors. It is becoming more true at the level of the grassroots, the general public.

This is not to say that people are content with their government, since as we have seen from a variety of elections they are obviously not. I do not think that the United States or any of us ought to crow like a rooster taking credit for bringing up the dawn. Nevertheless, a lot of organizations, the U.S. Baltic Council, Radio Free Europe, other groups in this room, Radio Liberty, our group, have been involved in pushing these ideas in the region for a long time.

The fact that the war of ideas is essentially over in this region is an important accomplishment and one that we should not lose sight of amongst all of the other things that maybe have not gone as well as we hoped.

In that sense though, I would argue that the war of ideas is not yet over in Russia or in the NIS region. The old dogmas of Marxism and Leninism are gone, and were probably only giving lipservice for a number of years. That does not equate to the acceptance of market economics and democracy for three basic reasons.

First, quite a few people simply do not understand what democracy is about. They know the word, but there is not a good understanding at a working level as to what the democratic process means.

Similarly, most people do not understand the basics of a market system or accept its most basic value, property rights.

In Russia and in the NIS, as opposed to Eastern Europe, relatively few have accepted or been able to operationalize or internalize the basic concept of a self-governing organization where people freely come together, form rules, and under the the laws of the society, are able to incorporate an organization, whether that be a firm, a political party, a trade association, a union, a Chamber of Commerce. That is a very basic problem when you are trying to do the kind of projects that we are talking about in Russia and the NIS. It really does distinguish, in our view, the experience we had in Poland, in Hungary from 1989 on, where these voluntary organizations proliferated. In Poland many grew out of the civic movement associated with Solidarity. That tradition is not present in Russia, and it is even weaker in other places.

Interestingly enough, Ukraine is an exception and a very good one. One of the bright spots in that country, is that voluntary organizations have begun to form. They have a better sense of direction probably because of the experience of the Western Ukraine, which was not under Russia for as long.

These points, I think, show that a lot of the debate or the discussion tends to be in my view a little clouded. Unless you step back and ask—what is the absorptive capacity of the societies that you are talking about, how can one begin to judge effectiveness or appropriateness or, indeed, even begin to create a strategy.

When we have looked at Russia, the NIS, these are the most difficult countries that we have to form private sector to private sector linkages. It has been very difficult for us to work with organizations that are coming together in the NIS simply because of the lack of this understanding of self-governance.

I will try to keep my presentation short and skip over some of the things I was going to say because they have either been said or may not be as relevant.

To give you just a sense though of what our strategy is, it is based on four or five key elements. First off, we believe fundamentally that, in these regions, politics and economics cannot be separated. Now, you may not need to have a wonderful understanding of structural adjustment and be able to sit down in trade theories of stabilization and exchange rates, but unless you can communicate in an effective way, it is going to be very difficult to make reform happen. The political will is not there.

So there is an intimate relationship here between politics and economics in every program in which we have been involved.

Second, our emphasis has been on key institutions, such as property rights, prices, and a regulatory environment. Only secondarily on the actual policy regime. That is

because of the history of this region, where the institutional base simply has not been there.

Again, in the same issue of our magazine we have an article by one of Douglas North's colleagues describing this phenomenon.

Last, stemming from my earlier remarks, our basic approach has always been to try to develop viable private sector groups that can play a key role in the advocacy process, both to craft policy reform recommendations and to build public support for their adoption.

Only secondarily are we particularly interested in organizations that will be able to carry out services to members like entrepreneurship training and other civil society type functions.

I could go on and on, but I think you can get the gist out of this.

The last point I wanted to make on the strategy area is that we ask a key question before we get involved in working in any country and certainly in this region. That is, No. 1, has the country made a firm commitment to a change in system, not just a change in the way in which the government might be structured, or are they trying to perfect or to rehabilitate an existing system.

Unless they have made a commitment to a change in system, it is much more difficult to talk about the kind of programs that we are doing.

And then, second, a corollary: does the public and private leadership of that country understand what that commitment means? And when one talks to many of the leaders of the Russian Duma or others, I think even today, there is really, I believe, not a real firm grip on the fundamental implications of what that change in system means.

I do think when you start doing projects in this area, particularly in Russia, as a first step one needs to look at the stock of institutions, the policy regime, the self-governing nature of the organizations. Look at what is there and avoid oversimplifying and making assumptions that might later turn out to be misguided.

For example, one assumption that people often tend to make is that because a company is in private hands, that means that you have got a private enterprise system, which is just fundamentally not true. That is a lesson that we have learned all over the world, and I think it is one that the United States is going to have to relearn in Russia.

So I would agree that you have to distinguish when you are doing projects, particularly grassroots projects, particularly projects where you are trying to build democratic structures for the basis of new political parties or trade associations, are you dealing with real private entrepreneurs; are you dealing with cronies; are you dealing with nomenclatura; are you dealing with fronts; what are you dealing with? A very basic question.

Another key point, at least one that we have run into, is that every one of these projects really has to be handmade. You have to develop a strategy based on what your partner organization wants to accomplish. You cannot dictate to them what that is. If you try, and I admit that we have on one occasion or two occasions early on made that mistake, we have learned it does not work. Unless it is their commitment, unless it is their program, unless they are prepared to put in some resources, it is very difficult to expect to get much in the way of results. This does imply, and I realize that many in the foreign assistance community will throw up their hands in horror at this point, these are much more staff intensive programs. They take a much longer lead time. You have to develop

a strategy, a management plan, a budget that accommodates that plan and is based on the reality of the country.

This puts you directly in contradiction to a lot of procurement regulations in the United States. It is very difficult to have a Request for Proposed (RFP) written by a small group of people who may not have the skills in all of the areas, to actually know what is involved in accomplishing the objectives that they have set out. Once that RFP is written, you are then in the position of responding to that RFP.

For that reason, we have not responded to a lot of REPs because when you look at the basic assumptions or the fundamentals of the management systems, it just cannot be done the way it is laid out. Nevertheless, one should not turn around and beat up the AID staff, in my view, because they are in a system where the procurement code is mandated.

We need to step back and take a different look and say, "We have got to have different approaches based on what we are trying to accomplish." These approaches need to be based on evaluating what kinds of approaches work and under what circumstances.

Procurement is one thing. Strategy, systemic change, political development, economic development are different things, and you do not necessarily get it through the procurement process.

The very last point I will make, and I am sure the Chairman will be happy to hear me say that, is that there was a very interesting article which I see you have here by Michael McFaul, in the Washington Times. I would encourage everybody to read this. I had actually written out very similar thoughts.

When the Congress looks at foreign assistance for the next couple of years, please start making the distinction between what the foreign government or the regime is doing, has done, and what our strategic interests as a country may be in developing assets and allies in the private sector.

And there are three reasons for that. One, you must distinguish between official thought and these private groups which represent an alternative to an official thought.

Second, work with new private groups gives you a window into a country that you cannot get any other way. You really cannot get it from just analysts or from having Americans stationed there.

And, third, and I think this is a lesson we have learned in Central Europe, is that these are the alternative governments. Working with private groups, even though we may decide we do not want to pursue government-to-government assistance is a vital step in building to the future.

It is a small investment because these are much less expensive programs, but it is one which can pay a lot of dividends later when they do have a transition.

On that I will end. Thank you, Mr. Chairman.

**Mr. Evans.** Thank you very much, John.

Well, we have had four excellent and, I think, very thought provoking presentations, reflecting several different perspectives, and I would like very much now to open this up to our audience. Many of you have been standing very patiently for an hour. I am sure there are a lot of questions. I hope there are.

When you do, we have a microphone there if you care to use it, and if you would state your name and affiliation, that would be helpful, but not necessary, and please direct your questions to the panel as you wish.

Yes.

**Mr. Murphy.** I am Dick Murphy with the Center for Strategic and International Studies, and this is a question for Mr. Dine.

Basically I would like his reaction to testimony given yesterday by my distinguished colleague, Zbigniew Brzezinski, to the Senate Appropriations Subcommittee on Foreign Operations in which he was highly critical of our policy toward Russia, characterizing it as naive and historically myopic.

And he offered a series of recommendations which, for the benefit of the audience here I will just summarize. There were four of them, and I would like Mr. Dine's comment on them.

First of all, United States policy should be more focused on the support and encouragement of democratic political parties and democratic political leaders in Russia, and he distinguishes between that and the personalization of support in the person of Yeltsin.

Second, a strong condemnation, a clearcut and forceful condemnation of Russian action in Chechnya, including the branding of the Defense Minister Grachev as a war criminal, and he suggested to give substance to that recommendation that some portion of the funds allocated for the construction of housing for Russian officers, say, 50 percent, should be diverted for relief in Chechnya.

The third recommendation was that notwithstanding Russian behavior in Chechnya, economic aid to Russia should generally be continued, although Congress should not hesitate to pull the plug out of projects which are either indirectly financing acts of organized violence or in cases where the Russian Government is failing to meet minimum standards of responsible conduct regarding financial accountability.

And his last recommendation was that in order to promote geopolitical pluralism in the space of the former Soviet Union, aid for Ukraine particularly and for the other New Independent States should be in all cases no less than that for Russia itself.

I would welcome your comments.

**Mr. Dine.** Thank you for relying on your colleague. I will go down your list.

In terms of United States policy having to do with political parties in Russia and whom to deal with in Russia, it is my belief, and I believe that it is true, that the U.S. Government has a Russia policy, not a Yeltsin policy. I know a lot has been made about the personalization of the Bush administration of Gorbachev and now the Clinton administration of Yeltsin, but I believe at the time that Mr. Bush and Mr. Baker also had a Russia policy, and certainly now we have a Russia policy.

You cannot deal with the United States of America without dealing with whomever is President and his advisors, as well as who is in Congress, and I think it is too glib, frankly, to talk about Yeltsin, Yeltsin, Yeltsin, not that there are not problems. Obviously there are, although he seemed to make a decent show yesterday in his State of the Nation address. (a) He got there. [Laughter.]

(b) He gave it. (c) It lasted an hour. [Laughter.]



There are people in this audience who work with political parties in Russia, as well as Ukraine and other NIS countries, particularly the International Republican Institute and the National Democratic Institute for International Affairs, and in the long run, I believe their work will show what this nation believes. That is, we are transferring a value, as well as particular technical skills, and I believe in the long run that will be a success that we can all take great pride in.

The fact that the people's money is behind those efforts through these two institutions is a credit to the Congress, as well as to the administration.

Does Russia need more? Of course, it needs more.

One of the things I disagreed with Brzezinski's testimony yesterday was that his premise is somehow or another in this myopia, as he called it, and in the illusion of policy and power and programming, that we do not know what we are dealing with.

Well, it is pretty clear from as different as all four commentaries were this morning, nobody believes that we are dealing with a bed of roses, particularly in the field of democracy and particularly what lurks over the horizon in terms of the communists still being in the Duma, but I am more concerned with right-wing, fascist kind of nationalism that lurks behind every rock.

At the same time we have got to be cognizant that this formerly nondemocratic country has made a commitment in its leadership and its peoples and its growing institutions to democracy, and it will not develop as fast as we all wish. I wish somehow or another our political leadership would get over the CNN and USA Today mentality of instant democracy, instant capitalism, instant social institutions. There is no way that Russia itself or external donors with Russians can produce instant anything in a society that is as sophisticated, as historically grounded and founded, and as cultivated and literate as it is.

Every time human rights are violated anywhere, we in this country need to speak up and speak up loudly. Brzezinski wants us to condemn or be more condemning of Chechnya. Whether we are or are not, I do not know of a soul that believes that this was a good thing. Chechnya was an awful tragedy, awful for those who are killed and maimed and left homeless, as well as awful for all of us who are trying to help Russia change 180 degrees, as I mentioned in my own presentation.

Foreign ministers, defense ministers, interior ministers or secretaries of defense, secretaries of state, and secretaries or administrators of the FBI or whatever, even the CIA, come and go, and that is up to the elected leadership of any country. So I do not agree that we ought to be condemning people per se.

What we are doing with the horrors and the atrocities of the Balkans is that the United Nations has put together a war tribunal group in The Hague, and maybe if that is what Brzezinski wants, let him do that, too, but I think you need more evidence about criminality if we really believe in the rule of law.

His third point being that economic aid to Russia should generally be continued, particularly in areas that are beneficial to both countries, and he specifically puts in brackets such as the Nunn-Lugar funds, well, obviously I think so. The United States Government today, as I tried to say earlier, and the United States Government tomorrow will be about institution building.

I agree wholeheartedly with one of the speakers, when he said we do not want to improve what is there now; we want to change the structures. We want to change the

institutions. Hopefully we can change the mentality, but I do not know how anybody does that, even if you had a foreign aid program of psychiatry. We are into national character and national behavior and everything goes with societal behavior.

So, yes, I think we need to continue to push ahead with all of the ups and downs. Every one of these countries, whether they are in Central, Eastern Europe, free Baltics, or the 12 former Soviet Union countries have got to push ahead. There are voices at this end of Pennsylvania Avenue that do not want to push ahead, that do not want to sustain the effort to bring reform, dramatic reform, radical reform to these countries.

And I do not know of anything that would be more intolerable and harmful to the United States of America than if we ended these programs or cut them dramatically, cut them down to low-yield margins. It is hard enough to do what we have been assigned and mandated to do by two branches of government since 1989. Both branches together have wanted us to join in with the Western Europeans and the international financial institutions to try to bring this dramatic change about.

And those who are calling for cutting Russia forever, cutting Russia \$100 million, cutting Russia here, cutting Russia there, put it in perspective. What do you want this world to look like 20 years from now? What do you want it to look like 10 years from now? And will it if you sit on your hands?

I have always been raised and believe that if you want to be a spectator, just sit in the seats at a bullfight. But if you want to be in the action, be a bullfighter. Get into the ring, and face the difficulties. The United States of America in this post-cold war period has to be in the ring publicly and through its PVO's, NGO's, and through its business communities.

So does the rest of the world. So do the Russians; so do the Ukrainians; so do the Armenians. And it is foolish to conduct a public dialog about ending it all.

Brzezinski's fourth point: it is essential to promote geopolitical pluralism in the space of the former Soviet Union. That means that aid for Ukraine particularly and for the other New Independent States should be in all cases no less than that for Russia itself. From your mouth to God's ear.

There is no Congressman or Senator I know of that is going to vote for more money this year, particularly.

The debate over the Marshall Plan, as I mentioned earlier, went on; it really was day after day because Marshall, and others, were up here all of the time, but they got many billions of dollars. I think the whole program at the end was \$300 billion in then-year dollars.

This is a pittance of what the United States is now spending and will spend. It is pittance when you add up the International Monetary Fund, World Bank, European Union, European Bank for Reconstruction and Development, and every individual bilateral donor program.

And if you are going to be serious, then you have got to put up the money. Yes, Ukraine is important. Yes, the other countries are important, as long as they want to be democratic and market oriented economies. At least four of those countries of the former Soviet Union do not right now, and I do not think we should waste our money on them.

But the big three in the area that I am responsible for implementing assistance in are Poland, Ukraine, and Russia. If those countries do not succeed in terms of the way

they want to succeed in terms of reform and we want to succeed in terms of our national interest, then you can kiss it all goodbye.

So I have my problems with Brzezinski.

**Mr. Evans.** Tom, thanks very much.

Next question?

**Mr. Iwanciw.** Eugene Iwanciw with the Ukrainian National Association. My question also is to Mr. Dine.

I think we are in agreement with you on your last point that the contribution of the United States and international organizations or allies is a pittance compared to the challenge that faces us. However, the President just sent up a budget, \$1.4 billion, for a part of the world that encompasses 450 million people, and it is the job of the President to lead, to propose, as he did for the NIS a couple of years ago with the \$2.5 billion proposal.

I think you cannot blame the Congress unless the President leads and the Congress fails to follow that lead.

But let me go beyond that. You had mentioned the importance of creating fundamental changes in these countries, and I think that is what is needed to have the long-term success. I am somewhat perplexed, and I will speak specifically about Ukraine with which I am most familiar, that numerous AID programs and other governmental programs are supporting not those groups that are initiating change, but the status quo groups.

We have money going to so-called NGO's that are little more than old line communist front organizations. The Department of Agriculture is spending a tremendous amount of money and some AID money is going to improve the productivity of collective farms rather than encouraging the privatization of land and private farmers.

The head of the Ukrainian private farmers was just in my office 2 weeks ago and said, "We cannot get the assistance from the U.S. Government. It is going to collective farms." When we improve the productivity of collective farms, of state managed and state owned enterprises, we are not doing what we set out to do in the FREEDOM Support Act of creating the fundamental changes for democracy and for the private sector.

One last point. We talk about, and I think two of the panelists raised, the need to go to the grassroots, and here again AID and the international organizations have looked at big projects. One case in specific: a proposal sitting at AID for over 2 years on the creation of credit unions which are local, grassroots, teach democracy in its very institution, and AID or someone at AID a year and a half ago said, "We are not interested. We are going to create big, commercial banks."

And so the big New York banks get the grants to go and set up a major bank which is not going to serve the needs of the small businessman or the individual consumer or the farmer, and the credit unions, which is proposed by the World Council of Credit Unions, which has a great track record in Poland, has been sitting for 2 years unfunded.

Now, I think those are some of the kinds of problems, and the bottom line is that a good part of AID money has not been going to achieve those objectives which you articulate today, which are spelled out in the FREEDOM Support Act.

Can you please comment?

**Mr. Dine.** I think there are three points. I will try to reply at least to three of them.

No. 1, the President leads, and the Congress appropriates. Well, I come from a school of thought which says if you want big changes, you have got to put up the money, but I am only one person, and I have only been on this job for 1 year and 11 days.

**Participant.** [Inaudible.]

**Mr. Dine.** Thank you, and I am so happy to have the next question as well. [Laughter.]

Before the big push in fiscal year 1994 for \$2.5 billion, the level for the NIS was about \$900 million, and it was deemed for fiscal year 1995 to send up here \$900 million. The 2.5 was a 1-year deal.

I wish it had been more, but that is just one man and one voice, and you can only go so far, and frankly, the Congress cut that by \$50 million. Fifty million dollars I have now discovered goes a long way, particularly when you are talking about grassroots programs, and I wish we had had that extra \$50 million for fiscal year 1995 which we are currently in.

The President just sent up a little over \$900 million for a whole slew of things, including trade and investment programs, but you know it is going to be cut, Gene, and that is too bad, too.

So you cannot separate, I believe. As you know, I am a student and a lover of the legislative branch, but you cannot separate in policymaking the two branches. One does have to lead in foreign aid. There is no doubt about it. That is the history. The President must lead. I agree with that.

But the Congress must lead, too, and they just cannot follow, and hopefully the partisanship that we are all seeing now can be mollified when it comes to these two important programs, that is the SEED Act and the FREEDOM Support Act. At least that is my hope.

So the \$1.4 billion for SEED and for FREEDOM Support looks like that is what the political climate will handle, and it may not even handle that. I am going to be working hard, and I know you will be working hard, and people in this room will be working hard for our foreign assistance program in general because you cannot have just SEED and FREEDOM Support. You have got to have it for the other parts of the world, as well.

Some of you I recognize in this room, and I did not see you very often when I was with my group standing at the doors of the House of Representatives and the Senate every time there was a foreign assistance vote. You cannot just have your program, and now I am preaching a little bit, but I have got a little experience.

You cannot get foreign assistance for your special projects unless you actively behave as citizen lobbyists, petition your government, and lobby for the whole thing. And the whole thing is very much fragile right now and vulnerable, and I hope not only the areas that I am responsible for working in, but the areas of Asia and Africa and Latin America are lobbied for also.

Your second point as I took it was why are we funding status quo groups, not change groups, change oriented groups. Well, I do not know how you label those. I hope we are not funding status quo groups. It really goes to your third point about credit unions and grassroots.

I, as I have learned in my short time in the executive branch, have very little say over the U.S. Department of Agriculture. I am totally opposed to anything that makes Stalin better. I want to kill, vanish every relic of the communist period because it is the

most demeaning system I have ever seen in my life anywhere, and I have lived in other parts of the world, and that is why I am so wholeheartedly on the side of reformers.

These are people who do want to do that, and we have got to be as a government and as a people on their side.

So if we are on the side of a few status quo groups, that is too bad, and I know a little bit about what you are talking about about the collective farms in Ukraine. I wish we were doing it differently, and thank you for the nudge, and it just reminds me that I should speak up even if I do not have any business to speak up, but I will speak up.

The need to go to the grassroots, your third point. Yes, I have seen the credit unions at work in Poland, and it brings tears to your eyes because, first of all, they look like credit unions. You walk in. There is not much room. It is just like going to the credit union of the House or the Senate. [Laughter.]

It is just people looking for a small loan or trying to deposit some money they never had before and probably will be wiped out by inflation, hopefully not if we can get the stabilization program moving so that it is not wiped out by inflation.

But some of the proposals I have seen with the credit unions in Ukraine face two problems. No. 1, there is not enough money, and for better or for worse, I am getting paid by you and all other taxpayers, and I guess that includes myself, to make managerial decisions in the allocations of moneys, and when you get down to when it is really tight, you have to choose one over another.

All of us have to do it in our own conduct of our daily lives, and you have got to do it as a manager of money.

I am a big fan of the credit unions, and they are change agents, and besides a whole new psychology, these folks need money, capital, small people getting small loans at very small interest rates so that they can pay them back.

If we were ever successful to double the size of this program, I assure you credit unions would be in it, but that does not adequately answer your question, but I cannot answer a lot of questions because a lot of projects are wonderful, but you cannot fund every one of them, and that is just a fact of life, and it is a sad fact of life considering how dynamic these societies are moving, how prosperous I think they will be, how in a generation or two they will be living very, very different lives in very, very different societies and be wholesome members of the international community.

**Mr. Evans.** We have had two very in-depth questions to Mr. Dine. Are there any questions for any other of our speakers?

Yes.

**Mr. Krikov.** My name is Krikov (phonetic), but I am with the U.S. Institute of Peace. I would like to direct my question to Mr. Kojelis.

There have been several references made to the linkages between U.S. assistance and U.S. security interests, not to mention the security interests of the region. In your opinion, has the U.S. assistance so far had any positive effect on preventing some of the tense situations that are occurring in the region, such as Moldova, Estonia, Hungary, Slovakia, from escalating into organized violence as has happened in other areas of the region?

And if yes, could you give some specific examples of that? And if no, do you have any recommendations or do you believe there is anything that could be done to help prevent the outbreak of violence?

Mr. Kojelis. Certainly our Coalition strongly endorses programs like Nunn-Lugar which will dismantle actual missiles and other systems. But the key issue, of course, is whether those countries will become democracies. You know, France and England have nuclear weapons, but none of us lose a minute of sleep over that because those weapons are controlled by civilian authorities that are popularly elected and democratic.

As Tom mentioned, the key issue is that Russia does not swing back into some sort of authoritarian, right-wing, or neo-communist kind of dictatorship, and once again. Also, you do not need a nuclear weapon to make somebody's life miserable as the people of Chechnya have seen.

So the fundamental link in our analysis on the national security issue is that of democracy building.

Let me describe our concern descriptively. We worry that AID funds are being managed by people who, as they come off the plane, shake hands with the first English speaking Russian they see, who tells the American consultant, "Yes, I am for democracy. Yes, I am for free markets. Yeah, I will be a recipient of an AID program or beneficiary of it," but then you look and scratch under the surface a little bit and you see that that person has no interest whatsoever, either does not understand what democracy and free markets are all about or purposefully subverts it.

We were meeting with a Hill staffer, a member of the House International Relations Committee, and he said, "You know, I think some of these leaders," and he was making specific reference to the Baltic States, "I think that they are purposefully leading U.S. assistance consultants along into a long period of muddle, as in Lithuania right now. All of the language to AID contracts is about democracy and free market, but all of the policies are very much more like those of the previous regime. They are trying to muddle along and lead the Western consultants by the nose. Once again, these consultants do know who was fighting the regime in 1974 and 1982 and who was part of the regime in those years. The nomenklatura has a purpose of keeping things muddled to that, they can aggrandize as many state assets as possible and do the "spontaneous privatization" whereby old communist bosses become new capitalists by absconding with big industries.

So this is our concern, and it is problematic for the domestic development of the Baltic States, but they are no threat to anyone. The problem is if those same consultants, or as Mr. Iwanciw from the Ukrainian National Association mentioned, are not able to differentiate between democrats and authoritarian-inclined people in Russia. The democrats in Russia are very, very, very weak. They are on the defensive right now.

We must help people like Elena Bonner. I doubt if any of the AID beltway bandit consultants know who she is or her history or Andrei Sakharov and others. I remember reading the story of Solzhenitsyn coming back to Russia last summer, and I was thinking what a profound event that was and what it might mean for the future of the region. Sadly, I also know the employees at AID. They are fine people who have worked many years in Africa and Asia. But they did not follow the tragedy and saga of Solzhenitsyn in the 1970's and before, and I wondered how many of them really appreciated the significance of that event. His return to Russia was such an important thing.

And I was thinking how many of those contractors over there do appreciate the significance of his return and know what it means, for good or for bad, for Russian democracy and, therefore, for the good or for the bad for U.S. security interest. Is it the Yelena

Bonniers of Russia that are going to have their, "fingers on the button" or will it be someone else?

You have got to be able to differentiate between a Elena Bonner and somebody else who is extremely glib and fluent in the language of democracy and free markets, but either does not really understand it or, as that Hill staffer said, is purposefully deluding you.

Mr. **Evans.** Yes, a question here.

Mr. **Murphy.** I am Brian Murphy with the Democracy Development Initiative of the Federal Bar Association.

And I want to thank the panel. Very, very informative.

At the International Judicial Conference held in Strasbourg in France in November of the past year sponsored by the U.S. Senate for Democracy, it was publicized that in Bulgaria the chief justice of the supreme court and the chief prosecutor were either ousted or about to be ousted by former communists.

This brings to mind the larger issue of support for judicial independence in the new democracies, and I am aware that the United States Information Agency is supportive of judicial independence projects and that AID has been in the past.

I wonder, Mr. Dine, and I hate to ask you again, sir, if you have anything you can share with us about the urgent need in my view to work on legal infrastructure, particularly working on supporting judicial independence in the new democracies.

Mr. **Dine.** Thank you for your question. It is a good one.

First of all, President Zhelev was here this week of Bulgaria, and if that man does not represent democracy and reform and the courageous past as well as hopefully a decent future, then no one does.

The USAID has several projects to help create an independent judiciary. In Russia particularly, the most clear-cut and visible that you can actually see is trial by jury. You know, if you read Brothers Karamazov, there is a trial by jury for the brother who has killed the father allegedly, but in 1917 or shortly thereafter that was ended, and it was a prosecutorial system thereafter.

So starting with Saratov and then going to nine other cities, Russia is now reinstating trial by jury, and we are providing training of judges both in this country, as well as at home; training of court officers. You go into, as I did, a courtroom, and now there are 12 seats for jurors, and it grabs you, and it is quite significant, and I believe Russians of many stripes like that.

Again, I come back to the same thing I said earlier to Gene. We could be doing so much more to help create an independent media. We could be doing so much more to help create an independent judiciary. We could be doing so much more in a variety of political, economic, social fields, but you can only do so much with what is there.

So I urge you, you know, in terms of your own organization, without Federal funding, perhaps to do a project or two yourselves so that it is PVO to PVO, NGO to NGO. I think that is the kind of thing that is going to take us through into the next century and beyond.

So there is some work going on. It is not enough, but little by little. Hopefully other European countries will be doing similar kinds of work, the French, the British.

Mr. **Evans.** Yes, a question back there.

**Participant.** I have a question for Dr. Sullivan.

You made a comment during your presentation that I thought was interesting and important, that just because an enterprise is in private hands does not mean you have a private enterprise system, and I was wondering, first, if you could expand on that point and, second, if you could say whether you think that the privatization program in Russia has been a success.

The reason I ask that is that statistics often get thrown around about the degrees of privatization and it is used as a measure of the success of our program, and even Mr. Dine mentioned in his presentation some statistics on different countries and Russia, in particular, saying that over 70 percent of property is now in private hands.

So could you expand on your comment and also address the Russia experience and whether it was a success?

**Dr. Sullivan.** Sure. Let me start just by rather glibly quoting, and I cannot remember which economist it was, who said if you scratch many business people, you will find underneath a monopolist.

I mean there are a lot of people in business, just like there are a lot of people in the human race, that are interested in cornering markets and doing a lot of other things. That is why a market system, as distinct from, say, the more crony type of system that one used to see—let me be precise—in the Philippines functions very differently.

You have a whole host of things that have to be put into place: contract law, property rights, antitrust law or competitiveness, as Europeans call it, things that instill and create competition between firms. We could go through fundamental principles of economics ad nauseam, but if you just pull out the basics and you look at it, those are the things that you have got to look for and say: are they there? If they are, are they constraining the behavior of these firms?

One indicator of societies where they are not is when you see huge interenterprise debt emerging, and that interenterprise debt begins to become a phenomenon of bail-outs. This is not a competitive enterprise system. It may be a system based on private ownership or private control of the number of firms, but it operates fundamentally differently.

Now, with respect to your second point, and, by the way, the EBRD, the European Bank for Reconstruction and Development, for all of their flaws in the past with their choice of marble, has done a phenomenal job of putting out what I think is an extraordinarily comprehensive report that came out just in November that lists the degree to which property rights, to use just one indicator, are present. Whether you are talking about intellectual property rights or other kinds of tangible property rights, is key to the degree to which markets are instilled in the various countries and the regions. So I recommend that highly as a better indicator than the number of private firms, although, of course, we think the number of private firms is absolutely important as well. It just is not the same kind of indicator.

The second point is on the privatization process in Russia. I think you have got to say: a success at what? You know, when we put that question privately to a number of leading Russians saying, why are you pushing it this way at this time, knowing what the likely outcomes will be, many of them made a point that is hard to argue against. That is that this is a political process of trying to break up the control points in the society to make it irreversible, to make it impossible to then put the system back together in the way in which it used to be.



Now, if you were to say has this process been transparent, clean, fair; has it resulted in world class competitive firms; are these firms beginning to restructure; do they have boards of directors; do those boards have effective managerial control; where is the ownership concentrated? When you look at those fundamental business or economic criteria, there are a lot of flaws.

So I think, again, you have got to keep in mind success at what? If one does take the view that the breakup of the nomenklatura system, so deeply imbedded in Russia, was a fundamental first step, which I believe was the point that Prime Minister Gaidar was articulating, then one would have to say that they have made some progress.

In terms of the more fundamental economic issues, there are a lot of reforms that have to be made before you are going to see anything remotely resembling really functioning, competitive firms.

**Mr. Evans.** Tom, would you like to comment?

**Mr. Dine.** Yes, I would like to also make a comment.

It seems to me your question also gets to the concept of what is privatization. To me privatization is not just the sale of state owned enterprises. Privatization is an ongoing process that may never end, has not ended even in this country.

If you will recall that the now Mayor of New York ran on a ticket of privatizing hospitals in New York City which he has still not accomplished. He has had a few problems.

What comes to mind quickly is an anecdotal story of the Vladimir tractor factory in Vladimir-Oblast. Three IESC volunteers, AID funded, went there, provided their expertise on how to deal with a nonprofitable, newly privatized firm. They helped develop a business plan, basic. They helped develop a corporate governance, what is the board of directors to do; what does it mean to be held accountable and to face an audit. They helped in selling tractors. What does sales mean, not meeting quotas, but sales and competing on a world market? Improving payment terms; accounts, management receivable; I mean these are basic tools, right?

Well, these three IESC volunteers provided their expertise, and it is a small story. You could repeat it over and over again, but we will never cover the whole landscape, particularly the smaller the business. Hopefully though the structure will be provided, the infrastructure will be provided. I do not mean roads and bridges. I mean the infrastructure of capitalism, of open, free markets, and that is what the American assistance program is about, as well as what the European Union is doing.

**Mr. Evans.** Yes. Thank you.

**Micah Naftalin.** I just wanted to make a few quick comments and get Tom's response to them. I was struck by two things in this discussion, and I have been struck with it for a long time.

It is clear the AID program is embattled. There is no question about it, and the calls for reorganization and the calls for reformulation of priorities or all of that is a very serious problem because the Congress, with the best of intentions, deals with organizational matters with a meat ax, and at the same time, when you are embattled, you are not going to be able to do serious reorganizing even if you wanted to respond to the tenor of all of these comments.

And I have great sympathy for you, Tom, because you have been there 1 year, and you have inherited a program that you have to defend institutionally, and yet you must know, and I am not going to even ask you, you must know that the concerns that are

raised, particularly with respect to the imbalance of the way in which AID organizes its support so that it loses the value of the people on the ground that know how to do the work; it is a fundamental problem, and you are not going to be able to solve it with the best of intentions in the timeframe of a budget cycle. It is impossible.

I was absolutely struck by the point. I wish I could have been able to say it over the years as eloquently as was just said a few minutes ago about the value of groups that not only are on the ground and understand it, but have a commitment to it so that they are going to stay there, as distinguished from corporate entities that move their resources from Latin America to Africa and to Russia or whatever.

It is the most important point, and it is the point, by the way, that the whole spectrum of people observing this program, and I am talking about NIS; I do not know anything about the rest of the world, but in the NIS everybody from the Heritage Foundation at one end to Mike McFaul and Carnegie on the other, to every NGO in this room or in this country or in the world that works in the field; everybody understands the same thing, that to make it work, you have got to work with the people on the ground who understand.

But it occurs to me that at the other side that is also the constituency for the foreign aid program, and it is those same people that need to be the lobbyists for this program, and indeed, they all will be, but it is a lot harder for the people that see the program and are worried that the baby will be thrown out with the bath, on the one hand, which is your problem, but it is also those of us who work at this level and see no serious way to break into the development of the program, and yet we are the people that have to sell this program to the Congress.

And, by the way, I will bet you every one of us has had conversations with Members of Congress in which we have been able to say after we listen to the AID bashing statements, when we explain what we want to do, they say, "Oh, yeah, well, that is OK. It is this other stuff I don't like."

So the problem is that the Beltway management firms are not very good lobbyists for foreign aid, and there has to be a way, it seems to me, even in the short run, recognizing that you have got a gigantic ship that you cannot turn around within a budget cycle; it seems to me there needs to be a way to somehow tax this gigantic program and come up with some initiatives that are more responsive to all of the critics, our type of critics as distinguished from the critics that want to destroy the program.

Somehow there has to be a way to send the signals that give the people who are trying to work with the Elena Bonners and Memorials and whatever. Those people feel like there is no way they can get moving, and if they cannot get moving, it is going to limit their ability to have a really good sense of how they can go and sell the program.

And, moreover, I think as embattled as AID is, if it could have an agenda for doing more of the grassroots stuff, of putting a higher priority on democracy, even though it said, well, we cannot afford it, you can have extra programs to be saying this is what you are going to lose in the Congress if you cannot rationalize this program better.

Anyway, maybe that is a long way of saying I would like to see a little more of your response to the two sets of comments that were coming from that side of the house and see if you see any wiggle room here to try to respond to it, even though I understand how embattled you are.

Mr. Dine. Well, thank you for your thoughtful points.

Yes, foreign aid as a concept is embattled, and so is the Agency for International Development, and I give Brian Atwood, the Administrator, a lot of credit because I do not think he is doing what he is doing and has to do in trying just to move organizational circles and squares and lines around. I think he is battling for a concept that is not popular.

Of the 13 appropriations bills every year, what are the two most unpopular? Foreign aid and the District of Columbia. [Laughter.]

And by the laughter, I think people get the point, and meat axes never solve——

**Participant.** Constituencies that cannot vote. [Laughter.]

**Mr. Dine.** Well, that is not true. You can vote.

**Participant.** No, foreign aid recipients.

**Mr. Dine.** Oh, you mean foreigners.

I am not deeply versed in corporate organizational life, but every time a meat ax is used in downsizing corporations, usually it goes sour, and I have seen it over the years in the Congress when somebody offers a 10-percent across the board, 5 percent. Then they are always back to 2 percent, and somehow or another that is good government.

That is bad government. It is a bad way to conduct the public sector, and it is a bad way to put together a policy, then a strategy, then programs and all kinds of tactical moves that one has to make to achieve objectives.

I understand the point about groups on the ground. I was a Peace Corps volunteer, and I will always be a Peace Corps volunteer, and I believe, as I said earlier, that you get things done at the ground and work your way up, but in this particular case, we are not just rebuilding Western Europe. We have been invited in by governments to help restructure, and that means first killing a past and then building a future.

And, consequently, there is a lot of attention, particularly by the press, to what goes on in Warsaw or Kiev or Moscow or Yerevan or Tbilisi, when in fact, the real thrill is outside those areas, but still if you are going to create small businesses in Vladivostok and Sabarask and other places far away, you have got to have a national structure, not more bureaucracy at the center. Listen to my words: a national structure. And that is why so much foreign assistance is going into that, and I think rightly so.

Now, how do we get to the grassroots? Well, through all of you is one way, and make sure our programs are that way. Yes, this is a big ship, and it does not turn very easily, and in my short time on earth, I hope I can turn it one, two, three degrees because over the course of time if you keep turning it that way, it will turn the full 360 degrees. But let's be realistic.

How do you break into the program? Well, again, I want to give my friend Brian Atwood a lot of credit. He has tried to come to an organization that was hide bound by congressional mandates, probably a couple I helped pass in my period; hide bound by congressional amendments on a yearly basis; hide bound by congressional political programs because each congressional office, senatorial office is representing their firm, their NGO, their corporation, and there have been quite a few breakthroughs in the managerial nature of AID.

If you look at just the contracts that the bureau I head has, it is not Beltway bandit heavy because we have done a computer run. Twelve percent from Northern Virginia and Maryland, and it is about 20 percent from the District of Columbia, but that is not an accurate figure if you look at it because there are too many Washington representational

offices that have signed the documents, but they come from Peoria and they are headquartered in Newark or somewhere else.

And, finally, we have gone out of our way, including my colleague Larry Byrne, who is the head of management, to try to get this reform through; gone out of their way to tell the people of Seattle and San Francisco and St. Louis and other places around the country we are trying to open this up.

**Participant.** [Inaudible.]

**Mr. Dine.** Well, you will see that there are more and more firms that have AID contracts now that did not a year ago.

Now, does it take an expertise to get inside? I think it does. Let's be fair. I am not going to B.S. you or me, but if you are going to comply to the Federal Acquisition Act and the procurement laws of this Nation, you have got to do it right. Otherwise you get your papers sent back.

Please, in my next life, never let me be a government contractor because it is a Sisyphus kind of situation, and you are constantly pushing the rock uphill, and only if the rock is small can you have any chance.

So there are problems, and they have not all been solved, that at least this administration is trying to do it with integrity and understanding the pain, the pain that you are going through and others are going through.

We have got to get more programs at the grassroots. There is no doubt about that, and with time that will happen, but it will require time.

**Mr. Evans.** Mr. Kojelis would like to say something on that point, and I would also like to ask Mr. Duss if he would after that?

**Mr. Kojelis.** Yes, I would like to say two points. Once again, this is something that I cannot emphasize enough, it is the review of the USAID contracting process.

Now, this is an RFP for a public administration contract (points to document on desk). This is a monster. This is a monster document, and I agree with you (Mr. Dine) that there have to be processes and systems in terms of Federal procurement. But when I look, for example, at what USIA or, say, National Endowment for Democracy require, in terms of procurement, and I assume that they are, following the congressional mandates and requirements and so forth, it is, one tenth the size of the USAID procurement document. Reduction in paper-work can be done because USIA is doing it and NED and other agencies are doing it.

And USAID must get away from regional grants. This RFP for public administration for Central and Eastern Europe; calls for contractors to be expert in handling everything from Estonia to Albania. I argue that that is just not possible.

So the contracting process must be changed. I do not know if you can appoint a blue ribbon commission or a group of malcontents like us——

**Participant.** Don't do that.

**Mr. Kojelis.** And I say the same things to any representatives of congressional offices. The devil is in the details, and the details are in these monster RFP's.

The second point is: why is this so important? Why is entry of new participants into the contracting procurement process important?

It goes back to a point that several people are complaining about here. We wish we could afford all of these programs. We wish we had more money. Let me tell you about

some of the costs that are actually involved. I will use some USIA cost figures. I was told by a friend of mine who has been very successful in getting contracts for internships to bring people over from Eastern Europe, and other countries, to the United States for 8-week internships. There was a little bit of a hubbub in USIA why this one NGO kept on getting these contracts as opposed to all of the bidders.

Well, he says it is because up until then a standard per capita cost for an 8-week internship in the United States was \$30,000 a person—\$30,000 a person! He says, “What a deal! I undercut them by half. I can do it for \$15,000.”

And this is a friend of mine. I did not tell him that I could do it for less than half of what he is charging, and given the volume, probably well under a third of what he is charging USIA for 8-week internships and probably even better than that.

But you have to apply free market principles to the contracting process itself. The more bidders you have on a contract to lower the cost permit of work. The USG should compare what a small NGO like ours can do, the number interns, the quality of programs, top level internships—with the big groups. We can provide, on a per capita basis much more product for the dollar as opposed to, one of the traditional contractors. That is going to extend that foreign assistance dollar. I can do it fourfold. I can do it at least fourfold if I am allowed to do the work and not have to grapple with that horrible contracting process.

So once again, what we are offering is a partnership. Our Coalition certainly is. We have a 15-point plan that does not require congressional legislation. We hope that senior people at AID take a look at it, and it would go a long way in solving problems.

**Mr. Evans.** Serge, would you like to comment?

**Mr. Duss.** Yes.

**Mr. Evans.** And then I think we will have to cut it off after that.

**Mr. Duss.** Yes. I think the contract situation is one thing, but despite the problems with monopoly on contracts, I think the major point that I would make that can be resolved rather quickly is on improving the quality of people who are managing these programs and making decisions on these programs at AID both in Washington, but especially in the field.

I am shocked at the naivety of many folks that come over, both from the government as well as the NGO community, who, as the salesman said in the Music Man, just do not know the territory, and they get suckered into partnerships with folks who really are nothing more than part of the old “operativi” who speak English rather well, are rather glib, and really are nothing more than the same old system, but wearing a suit that fits rather than the old timey cardboard suits. [Laughter and applause.]

The other problem is the attitude of people who come over, and this is also a cultural problem, is Americans who are very generous, but again very naive, who take the attitude of they are just like us.

Well, if the folks in the NIS have spouses and children, then, yes, they are just like us, but otherwise they are totally different, and we have to recognize this, and the decisionmakers also have to recognize this, as well as PVO’s who implement programs also have to recognize this as well to understand the political, the economic, especially the social condition that we are dealing with because changes will not take place over a generation, but over several generations.

One other point. I caution everyone when they use the word "success" in terms of U.S. assistance to the NIS especially, we cannot measure success in 1 year or 2 years. We can measure progress, but we cannot establish standards for success right now. We will be able to establish that five, possibly 10 years from now.

Progress, yes, but success at this moment, no.

**Mr. Dine.** I can end on an anecdote based on what you just said, and it is an important cultural comment, and I think the fact that the knowledge base among the societies we deal with over there and our own are really quite ignorant.

A mayor of a small town in Slovakia at a dinner party one night wagged his finger at me and said, "You've made mistakes, and we've made mistakes."

So, of course, I wanted to know what he had on his mind. He said, "When the Wall fell, we expected you to come in here with big, black satchels filled with cash and that you would throw your arms around us and embrace us, and you came in here expecting to find yourselves, and we aren't you and you aren't us, and we have got big problems."

But the challenges are worth it. Thank you.

**Mr. Evans.** Well, we could go on, but we have overextended our time. I want to thank our four panelists for very excellent, thought provoking, and stimulating presentations, and I would like to thank all of our audience for their questions, too.

This briefing will be published in due course, and anybody who is not on the Commission's mailing list who would like to receive a copy, please see me or one of our staff afterwards.

We will also be holding other briefings in the coming weeks. Again, if you are not on our mailing list, please see us about that.

Thank you very much. It has been a very good panel.

[Whereupon, at 12:07 p.m., the meeting was adjourned.]

## APPENDIX

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### USAID'S MISSION IN THE NIS: BUILDING AN ENVIRONMENT FOR PROSPERITY:

Thomas A. Dine  
Assistant Administrator for Europe and the N.I.S.  
U.S. Agency for International Development

The countries of the former Soviet Empire are in the midst of an historic transition from totalitarianism to democracy, from central planning to free markets, from isolation in a stagnant bloc to integration in the global community. Since 1989 in the countries of Eastern Europe, and since 1992 in the former Soviet Union, the United States has been an active partner for these 26 countries transition.

Stated most directly, our goal -- and our challenge -- in the the entire region is to help create an environment for prosperity.

By this, I mean collectively the institutions and structures, the patterns and habits, which make up the foundation -- the *sine qua non* -- for entrepreneurship, competitiveness, and successful private market activities. In other words, we are helping the countries in transition to establish the political and economic settings in which they can thrive and become fully integrated members of the global community.

A recent article in The Economist reviewing the bicentennial edition of Edward Gibbon's classic Decline and Fall of the Roman Empire put the point well when it noted Gibbon's core view "that free institutions, public service and active

civic spirit deployed to social ends are the lifeblood of the properly-ordered commonwealth, the fundamental preconditions for peace, harmony and material progress."

USAID is trying to help the countries of the crumbled Soviet Empire rebuild themselves, one-by-one, as democratic, market-driven commonwealths and join the broader commonwealth of free nations.

This U.S. foreign policy mission is an opportunity of extraordinary magnitude. In my view, the magnitude is matched only by the postwar Marshall Plan. As the 21st century approaches, we at USAID and other federal agencies, in cooperation with other international donors and the private sector, are playing an essential role in expanding the zone of freedom and prosperity across the entire Eurasian landmass, from Warsaw to Tirana, from Tallin to Vladivostok, from Chisinau to Yerevan and Almaty.

Meeting this challenge is squarely in the U.S. national interest. Having invested billions of dollars in the Cold War containment of Soviet expansionism and in competition against the Communist bloc, the U.S. consequently has a huge stake in the success of democratic transitions across Eurasia.

It is in our vital security interest that any nuclear systems in N.I.S. countries be dismantled in accordance with international agreements, that their military sectors be downsized, and that all the countries in the region become law-abiding at home and peaceful abroad. It is also strongly in our



economic interest that these societies become countries of middle-class consumers, that they become both reliable trading partners and sound investment opportunities, and that they become integrated into the global economy as quickly as possible.

The essential American interest is to promote and inculcate values such as the rule of law, individual rights, free and fair trade, democratic capitalism.

For the peoples of the region, all of this means a radical political and economic transformation. A 180-degree change. It means, first, undoing the Communist legacy -- the decades-old failed "experiment" that wrought such great damage and suffering, that warped national economies, and that isolated these societies from the march of human progress.

It secondly means the transition from patterns of stagnation to avenues of prosperity. This is a long-term proposition; it involves fundamental structural changes. Psychological as well as material obstacles make this transition bumpy, cumbersome, troublesome, often unclear. There will be severe dislocations. It will be costly. But thorough-going transformation is necessary, because it offers the only realistic prospect for a better future.

Radical change is not only in America's interest, it is also in the vital interests of all the Eastern European and N.I.S. countries. The transition to business-friendly societies is a "win-win" situation for all those involved.

In the spirit of full disclosure, I must confess that I am optimistic about the economic development and long-term prospects of many of the countries in the region.

In Central [and Eastern] Europe, the Czech Republic, Poland, Hungary and even Slovakia have made enormous economic strides. So successful have been the economic reforms in the Czech Republic since the "velvet Revolution" -- spearheaded by President Havel and Prime Minister Klaus -- that USAID has already announced "graduation" from that country by the close of 1996. Poland's economy grew at a robust 4% in 1994; it is expected to produce 7% real growth this year. Hungary has attracted over \$8 billion in foreign investment, mostly from the U.S., Germany and Austria. Despite political tensions in recent months, Slovakia continues to register steady economic improvement: for example, Slovakia achieved a \$200 million dollar balance-of-payments surplus in 1994, and its growth rate is targetted for 4% in 1995.

Performance in the Southern Tier -- including Romania, Bulgaria, Albania, Macedonia, and Slovenia -- has been less consistent. Slovenia is a candidate for early "graduation" from USAID assistance. Romania, which finally turned the corner toward positive economic growth in 1994, is at the brink of embarking on a mass privatization program. I consider Romania to be a "dark horse" favorite.

The three Baltic republics are doing well. Russian troops are out. USAID programs in Estonia will end in 1996. Latvia is

in line for "graduation" in the near future. Lithuania is closely linked to the Polish success story.

Among the New Independent States of the former Soviet Union, I am bullish about Russia and Kazakhstan, two energy and natural resource giants; and Moldova and Kyrgyzstan, two small countries with large potential. To this list, I would add the coming wave of reformers: Ukraine, Georgia, Armenia, and potentially Belarus. These are the new "front-line" states.

Armenia has been distracted and weakened by armed conflict and trade embargoes enforced against it, but Armenia is a very promising place. In the words of World Bank officials, "something is happening" in Armenia.

Ukraine once represented the object lesson that embracing old ways would get you nowhere. Today, thanks to the strong leadership of President Kuchma, Ukraine has embraced change and restructuring. The rapid international response this winter in support of Ukrainian reforms is putting that country on the road to national recovery.

I remain optimistic about Russia. Huge economic energy and vitality are being unleashed there. Fundamental institutional changes have been accomplished. Free markets have taken root and are growing, both in the central areas and in the regions.

We have learned that the path of transition is not always a straight line. There is no question that, politically, Russia today finds itself in a "time of troubles," as periods of potential upheaval have been known in Russian history. The

challenge of true multi-ethnic federalism is obviously daunting. The resort to force in Chechnya is a national tragedy.

But I believe one must put these troubles in the context of the great distance Russia has come -- politically, economically and socially -- since the collapse of the Union of Soviet Socialist Republics in 1991. Behind the terrible bloodshed in Chechnya and the news of power struggles in Moscow lurks a country of huge economic potential. Equally important is the fact that democracy is taking root, and the Russian state is no longer above public scrutiny. The Fourth Estate is doing its job. The free media are openly and vigorously covering the events in Chechnya and criticizing the government's war policy, as are many political parties in the parliament. As Stephen Rosenfeld of The Washington Post recently put it, this is not the time to write off Russia.

True, direct foreign investment and trade are still lagging, and recent events have likely dampened investor enthusiasm in the short term. Total direct foreign investment in Russia since 1992 amounts to only about \$2 billion, but institutional investors are beginning to enter the Russian market. During his summit meeting with President Yeltsin last September, President Clinton announced a \$100 million trade and investment initiative through OPIC, Ex-Im Bank, and the Trade Development Agency (TDA) to prime the pump.

Trade and investment do not happen in a vacuum. Trading partners must be reliable; the commercial setting must be right

for investment. The possibility of mutual profit must be real. In a very real sense, trade depends on aid.

USAID -- in coordination with the Departments of State, Treasury, Commerce, and Energy, USIA, EPA, the FBI -- and in collaboration with other G-24 members -- is actively assisting Poland, Romania, Ukraine, Russia and the other reforming countries to create open, dependable business-oriented environments -- economies in which domestic investment and foreign private investment will make business sense and will eventually become the primary sources of growth capital. Helping to build this environment for prosperity is our goal at USAID; it is our mandate from Congress and President Clinton.

We are concentrating our assistance efforts on institutional and structural changes that go to the heart of economic and political life in these countries -- changes that will be irreversible. Our budget is, of course, increasingly limited; therefore, we are focusing on areas where our technical input can make the biggest difference.

Conceptually, let me stress three themes of our approach: (1) targeting reformers in reforming countries; (2) helping private entrepreneurs; and (3) promoting wholesale structural changes in the political, economic, and social systems. These thrusts are mutually reinforcing and contribute directly to an environment for prosperity. Let me briefly discuss each one.

First, targeting reformers in reforming countries. It is clear that these countries have no viable alternative to reform

and restructuring. The longer economic reform is postponed, the deeper stagnation sets in. The reformers are the performers.

USAID supports the activities of key economic reform leaders, both at the highest levels and also at the grass-roots. American expertise is assisting reformers do their job. For example, we work closely with Russia's First Deputy Prime Minister Anatoly Chubais, formerly head of the State Property Committee (the GKI). Mr. Chubais and his proteges are the Adam Smiths of Russian reform economics. We are also working with Ukrainian Economics Minister Roman Shpek, whom President Kuchma tapped to be his agent to help lead an independent Ukraine out of three years of decline.

The second key theme is private entrepreneurship -- the driving force -- the turbo-engine -- that will sustain market reform. Privatization is the foundation, the critical element in the overall transformation process. This is where most of U.S. foreign aid -- the catalyst for this change -- is being directed. Over the last two years, \$200 million of U.S. technical assistance has been spent to support Russia's first stage of privatization, the voucher phase. Without the process of privatization taking root, I would contend, neither investment nor trade will occur in significant amounts.

In December 1991, when the Soviet Union dissolved, private entrepreneurship was not a major item on the economic agenda. Price controls and stabilization were. Two-and-a-half years later, Russia has accomplished one of the greatest political and

economic feats in modern history: via voucher privatization and auctions of small businesses, both sponsored by USAID, Russia has conducted the biggest sell-off of state property the world has ever witnessed.

The privatization program has resulted in, quite literally, the dismantling of communism, the undoing of state ownership of the means of production, the end of the command economy. More than 70% of the country's productive property -- comprising 20,000 large enterprises and about 100,000 small businesses -- has been transferred into private hands. Over 40 million Russians are now shareholders in private companies and mutual funds, more than in all of Western Europe.

As a result of this transformation of ownership, most Russians -- about 78 million people -- now work in the private sector. Markets have sprung up from Petersburg and Nizhnii Novgorod to Novosibirsk and Khabarovsk; markets for machine tools, markets for stocks and bonds, markets for equipment ranging from tractors to computers. Enterprises are responding to the new forces of supply and demand -- with product diversification, quality improvements, and higher efficiency.

The new entrepreneurs have created a growing constituency for more change: owners and consumers alike come to see their interests in the expansion of markets. A growing majority of Russians has a stake in the market and in the success of reform. Uncertainty about the future still abounds; yet people are seeing the market place not just as a source of instability, but as a

source of goods and services, of jobs and income. In people's minds, the corner is being turned. Russia is becoming "middle-class."

In order to speed the growth of private sector entrepreneurship in Russia, USAID has established two capital funds, the Fund for Large Enterprises in Russia (FLER) and the Russian-American Enterprise Fund (RAEF). These funds offer equity and debt financing, technical assistance in business planning, and links with Western sources of technology and investment. The U.S. has also contributed to European Bank for Reconstruction and Development (EBRD) funding for venture capital and small business development.

Linked with privatization is the issue of defense conversion. Many state-owned enterprises in Russia were -- and still are -- dedicated to military production. An important goal of Russia's overall economic transformation through privatization is to "civilianize" the economy, to reorient the once gigantic military-industrial complex toward consumer-driven, civilian production. By dismantling its command economy, Russia is creating an environment in which defense enterprises will have strong incentives to convert and produce things that regular consumers will buy.

Through the Pentagon's Nunn-Lugar program -- and specifically its Defense Enterprise Fund -- promoting defense conversion is a priority item for U.S. assistance to Russia. But conversion is only one part of our larger program and should not



be confused with the whole -- which is to foster a broad and lasting framework for systemic transformation.

Despite massive progress, private entrepreneurship cannot be taken for granted. We will continue to face both "active" and "passive" forms of resistance to change: for example, political opposition from status quo forces in the Russian parliament. Active opposition, for example, is stronger on agrarian land reform. As for passive resistance, the weakness of popular knowledge of how free markets work hampers reform. Public education needs are great. New economic habits form slowly. The vocabulary of change needs to become common currency. And in the interim, we need to take advantage of windows of opportunity for reform, such as the strong support to privatize urban land under the jurisdiction on many reformist mayors.

This brings me to the third key theme of U.S. aid to the NIS and other former Communist countries: promoting and inculcating structural change. Genuine structural reform is the all-important systemic link between politics and law, on one hand, and economics and business, on the other.

A business-friendly environment depends upon the rule of law, upon a well-ordered institutional and regulatory framework, upon the predictability, transparency, and enforceability of norms of commercial conduct.

For the first time in its history, Russia has embarked on the creation of what political scientists call a "civil society" based on law -- the idea that a vigorous private sector can

coexist with a principled, regulatory state. The Communists viewed law as a blunt tool for enforcing the command economy -- and their own positions of power. But law, broadly understood, is in fact the glue that holds complex modern societies together -- law is both liberty and responsibility; it is both the free market and sound regulation.

USAID will continue to pair American experts with their East European and N.I.S. counterparts to design and implement new legal systems, including constitutional reform; civil and criminal code reform; labor code reform; new banking, bankruptcy, and antitrust laws; fair tax and intellectual property laws.

For the next few years, USAID assistance is specifically aimed at:

- developing capital markets, establishing equity and commodity exchanges, and other trading infrastructure;
- establishing responsible regulatory agencies (for example, analogs to our Securities & Exchanges Commission), as well as practices of commercial self-regulation (such as we have on the New York Stock Exchange and the NASDAQ);
- instituting modern financial accounting standards;
- developing rules and standards of corporate governance;
- drafting modern commercial laws, such as the first part of the new Russian Civil Code, containing many of the basic commercial laws, which went into effect on January 1, 1995.
- overhauling the irrational taxation system to establish a clear, fiscally sound, and non-punitive tax regime;
- passing comprehensive land reform.

These new institutions, once well rooted, will contribute to a business-friendly environment for prosperity.

Students of history learn that modern societies evolve from "status" to "contract," meaning that, in primitive economies,

business is governed by personal status and contacts, while, in advanced societies, contracts and arms-length deals rule the day. A hundred years ago, Count Witte, the Tsar's minister, wrote that Russia had "no sense of property or legality." Things only got worse in the Soviet period under the *nomenklatura* (the Communist ruling class). Today, the successor states have emerged from darkness and are gradually -- but surely -- entering the world of contract, of markets, of respect for individual rights. Indeed, there is a whole new social contract.

As this new social contract develops, Russia and other former Communist states must contend with the legal and institutional void that has opened a door to crime, in particular organized crime. Crime is one of the biggest obstacles to economic progress in the East. President Yeltsin has asked the U.S. Government for help in counter-attacking crime and corruption within the Russian government and the new business classes. On the law enforcement side, agencies such as the FBI are working with Russia and other countries in the region to devise credible strategies to reduce and prevent economic crime. On the law implementation side, USAID is working with judges and lawyers to ensure that they are prepared to administer efficiently and fairly the new rule of law. Success in these efforts will be good in itself, but it will also serve to reduce the perceived "country risk" of doing business in Russia, which deters eager foreign investors.

In sum, USAID is trying to be a partner for change with the

reforming post-Communist countries, to be a catalyst for bringing about an "environment for prosperity." That will benefit both the citizens of the NIS and American business interests. Through targetted economic assistance, USAID is:

- Supporting reformers efforts to achieve real structural change.
- Building a constituency for that change.
- Helping to open up the diverse new business opportunities to the world market.

Moreover, USAID can play this role effectively, and then exit. Before the century ends, I believe the results in Central and Eastern Europe -- as well as in the N.I.S. -- will match, if not exceed, the results of the eleven-year Marshall Plan. And the West will have "won" not only the Cold War but -- more important -- the peace that followed.

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Remarks of Serge Duss  
Associate Director for Government Relations  
World Vision Relief and Development

Commission on Security and Cooperation in Europe  
Briefing on  
"U.S. Assistance to Central and Eastern Europe  
and the NIS: An Assessment

February 17, 1995

Thank you, Mr. Chairman, for the opportunity to contribute brief comments as we try to assess United States assistance to central and eastern Europe and the Newly Independent States of the former Soviet Union. Since my specific area of expertise is the Newly Independent State, I will limit my comments to that geographic area and focus on a grassroots perspective on U.S. aid.

Living and working in Russia for almost three years, arriving in Moscow only weeks after the attempted coup against president Mikhail Gorbachev, allowed me to witness an event several months later very few thought would take place in this century: the termination of the Soviet Union as a political state. However, the question of dissolving a Soviet welfare state-culture molded over 70 years and three generations and whether it evolves into a civil society where a free market flourishes is quite another issue.

At the start, the U.S. assistance program to the NIS, particularly Russia, was well intentioned with its emphasis on promoting a market economy and fostering an emerging civil society. However, the U.S. rush to demonstrate support for, and solidarity with, the new fledgling Russian government resulted in two major problems which dog the program to this day:

1. Russian reformers and reform institutions were unable to responsibly absorb the aid, more than \$1 billion in FY94; the legal and civil infrastructure to accommodate privatization, for the most part, is not yet in place. Eventhough companies may be privatized on paper, they are still controlled by Soviet-era directors and operated along the principles of a command economy and resistant to change.

Small businesses, the key to any thriving free market economy, appear to also have missed out on substantial foreign aid. A recent poll conducted by the Center for Economic Reform in Moscow revealed that only 0.3 percent of the small businesses surveyed across Russia (just five out of 1,628) had managed, through the help of professional associations, to get any international assistance.

In addition, too much emphasis was placed on short-term results -- jump-starting the economy, rather than long-term. Nothing is ever jumpstarted in the former Soviet Union.

2. U.S. aid money was disbursed to agencies and contractors that were ill-prepared to achieve the objectives of the assistance program. One pool of well-prepared groups that could have been utilized for project implementation in the NIS, particularly Ukraine and the Baltic republics, was American ethnic organizations. These organizations are comprised of professionals who speak the language fluently, understand the culture and are committed to the long-term. But they were never approached for assistance.

In addition, before the Bureau for Eastern Europe and the NIS was created at USAID, layers of bureaucracy were actively involved in the decision-making process for grant approval.

It's my observation that U.S. assistance programs that focused on the grassroots -- the common people -- derived the greatest payback on its investment. Programs that seek to build and strengthen civil society through the development of a variety a citizen voluntary organizations, including self-help associations, empower those in post-Soviet society who have never before had the right to govern their own communities.

Programs that focus on management training, education about democracy, rule of law and free markets inspire and empower formerly powerless people to think for themselves and begin to resolve their own problems by utilizing available resources.

One of the USAID-funded programs which World Vision implemented focused on initiating reform in the Russian nursing education system. In two years, Russian nurse educators overhauled their approach to nursing education. They adopted a new philosophy of nursing, free of Marxist-Leninist ideology, that will enable future generations of nurses to care for patients as people -- complete with body, soul and spirit -- rather than numbered objects. Reforms adopted by Russian nurse educators are now being institutionalized country-wide through new nursing associations being developed in major cities around Russia.

As the U.S. government funding begins to decrease to the NIS, programs should begin to focus more on developing a democratic infrastructure -- strengthening civil society -- by training and educating present and potential leaders in communities.

What we must understand is that a social revolution is just beginning to take place in Russia, the Baltic Republics and Armenia, and less so in the other NIS republics. Communities and individuals conditioned to subservience to the state are for the first time dealing with choices, and for many it is a scary experience.

We also should understand that U.S. assistance, in fact, all Western assistance to the NIS, but especially to Russia, is merely a stimulant for free market development and civil society. Therefore the U.S. must use diminishing resources to till and cultivate the grassroots so that whatever seeds of aid are invested will be nourished by communities to develop and promote trust, fairness, cooperation, tolerance and inclusion.

I would suggest that during the remaining years of the U.S. assistance program it focus more on smaller scale privatization -- the shop keepers of NIS -- and target sectors of society that will impact the largest number of people.

1. Help rebuild educational systems. Schools are starving for new textbooks and curricula free of communist ideology. Funds should be redirected to create books, videos and films that explain democracy, free markets and political, ethnic and religious pluralism.

2. Enthusiastically support legal reforms. Legal systems in all the republics continue to reflect the arbitrary nature of Soviet justice. Legal reform programs should be strengthened. Support must be provided for building an adequate court structure and creating legal associations.

3. Significantly increase the number of exchange programs for NIS students and budding community, political and business leaders. And let's not be shy about incorporating the study of ethics and the vital role of moral values in civil, democratic society.

In Russian there is a single word that characterizes all of the envy, hate and tired mediocrity of the Soviet legacy. The word is "sovok." It's a slang term derived from "sovyet", as in sovyetskiy soyuz ... Russian for Soviet Union. An 1992 article in one of Russia's first independent newspapers Nezavasimaya Gazeta described a sovok as a person with "a crazed thirst for equality, a deep hatred for the success of others, and a flourishing laziness."

Ultimately it's the sovok mentality that stands as the greatest obstacle to political and economic reform and the steady emergence of civil society and democratic institutions. Only as U.S. assistance programs -- in business, government and social sectors -- are able to help citizens of post-Soviet republics shed the sovok mentality, can we have any real hope of long-term success in the NIS and achieving its goals for the benefit of future generations.

# STATEMENT BY LINAS KOJELIS

on behalf of the

CENTRAL AND EAST EUROPEAN COALITION

before the

COMMISSION ON SECURITY AND COOPERATION IN EUROPE

February 17, 1995

Mr. Chairman:

I am pleased to speak on behalf of the Central and East European Coalition<sup>1</sup> on U.S. government assistance to Central and Eastern Europe (CEE) and the Newly Independent States (NIS) of the former Soviet Union (FSU). It is, after all, this committee which, for decades, has focused on and studied the fundamental issues which should be at the heart of U.S. assistance to this region -- human rights, democracy and free markets.

The U.S. assistance program of the past five years and for the foreseeable future should have been a dream come true for that cluster of individuals and organizations which we can call the "Democracy/Human Rights Community." This is the community which worked side by side with this Commission -- organizations like Helsinki Watch, Amnesty International, Freedom House and a host of others -- in the long hard struggle against totalitarianism in the CEE and FSU. All of the members of our Coalition are charter members and veterans of the Democracy/Human Rights Community. We, like you, know fully and understand deeply the wholesale harm done to the countries of the CEE and NIS by communism and the excruciating pain and difficulty of the current democratic transformations. We have worked side-by-side with you for the past two decades and will be working with you far into the future.

For organizations like ours, the waste, fraud and abuse which have become the hallmark of U.S. assistance to the CEE and NIS countries is ironic and painful, indeed.

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<sup>1</sup> CEEC member organizations include; American Latvian Association, Inc.; Armenian Assembly of America; Belarusian Congress Committee of America; Bulgarian Institute for Research and Analysis; Congress of Romanian Americans, Inc.; Czecho-Slovak Council of America; Estonian World Council, Inc.; Hungarian American Coalition; Joint Baltic American National Committee; Lithuanian-American Community, Inc.; National Federation of American Hungarians; Polish American Congress, Inc.; Slovak World Congress; Ukrainian Congress Committee of America, Inc.; Ukrainian National Association, Inc.; and the U.S.- Baltic Foundation.



Everyone in the Democracy/Human Rights Community understood the joy of learning that another hand-typed issue of a *samizdat* publication had been successfully smuggled to the West or the anguish in hoping that a letter or a package to a prisoner of conscience in the *gulag* might actually be received by the addressee. In those hard and dark years, there were no fat U.S. government contracts to promote democracy, human rights and free markets in the region -- we did it all dissident by dissident, dollar by dollar.

I will not try to recount the never-ending list of criticisms of U.S. assistance programs chronicled regularly by the media. Anyone with access to an on-line media data base simply needs to key in the phrases "U.S. assistance," "Central and Eastern Europe," "former Soviet Union" and "waste" and then harvest a bounty of articles, reports and studies documenting the problems. We are including, as an addendum to this testimony, four such articles from *The Wall Street Journal*, *U.S. News and World Report*, and *The Washington Post*.

The squandering of hundreds of millions of dollars of precious democracy and human rights development funds is beyond words. What exactly has gone wrong with the process and what can we do to change it?

The problem began at the very start, the moment Congress appropriated the first substantial funds (now called SEED and FREEDOM Assistance Funds). The management of these funds was overseen not by the veterans of the Democracy/Human Rights Community but by government technicians and bean-counters and a host of generic international development, fee-for-service contractors, almost none of whom had the least bit of experience in the fight for freedom in the CEE/NIS. The Democracy/Human Rights Community was not even consulted in the design of these programs.

The disenfranchisement of this community of dedicated and knowledgeable experts from the design and management of U.S. assistance programs for the countries of the CEE/NIS is, without question, the most fundamental reason for the tragic waste of hundreds of millions of dollars over the past five years. Consequently, the dire need to integrate the Democracy/Human Rights Community into all current and future programs should be a top priority of this Commission and this Congress.

A second vital issue is the contracting process of U.S. assistance agencies, especially the U.S. Agency for International Development. Issues related to this process are extremely byzantine and cumbersome. However, they are also critically important to the purpose and success of U.S. assistance to this region.

To date, Congress has shown much greater interest in the total sums of dollars appropriated for the region, than for the processes by which this money is actually transformed into concrete assistance which is often not appropriate to or meets the specific needs of target countries. Our friends on congressional staffs sadly admit that their eyes glaze over when we begin explaining the technical details. Others have even berated us for wasting their time with such matters. But the bottom line is that the failure of Congress to focus on the details of the contracting process guarantees the continued mismanagement of a huge proportion of these funds.

Our Coalition prepared a fifteen point plan to reform this arcane and wasteful process. These reforms include:

- \* Ending CEE or NIS region-wide contracting processes which fail to reflect the specific needs of individual countries;
- \* Requirements that contractors have specialized knowledge in the region; requiring that U.S. government program designers use knowledgeable experts in the design of programs;
- \* Requirements that contractors have a long-term commitment to the region which will transcend the U.S. government funded work;
- \* Routine public disclosure of the specific tasks, goals, and funding levels of USAID contracts;
- \* Ensuring an open and fair process for awarding grants and contracts; and
- \* Streamlining and simplifying the contracting process to encourage entry by smaller, region specific organizations.

These are all common sense solutions, and our Coalition is wholly bewildered by the vociferous opposition by the Administration to these simple reforms.

Without question, the one provision the opponents of reform fear most is the requirement that contractors have a **long-term commitment** to the region. Quite simply, this requirement would eliminate over 90% of the pretenders to these scarce funds.

This requirement goes directly to the question of which organizations and individuals have a solid track record which proves that they **know and care** about the fundamental issues involved in the reform of post-communist societies. Are they the gaggle of "Beltway bandits" or generic international service PVO's which aimlessly search the pages of Commerce Business Daily for the next fat federal contract to come along? Or are they the ones which have been hard working partners of this Commission for the past two decades and which will continue their commitment to strengthen human rights, democracy and free markets long after the last USAID office shuts down in Central and Eastern Europe and the former Soviet Union?

It is no accident that right now a debate rages in Congress about returning control of local programs to local governments because running them from Washington has simply not worked. This is our recommendation exactly: use Region Specific Organizations, including many in our ethnic communities, in the assessment and delivery of U.S. assistance. Why? Because we know the area, the language, the people, and the pitfalls. Because we represent a range of American private sector interests - business, humanitarian, religious, social, cultural and other - who are investing tens, and soon hundreds of millions of private sector dollars, in-kind donations and volunteer services into this region and we want to see it succeed. Because we are NOT there for the short haul or the fast profit; we and our

children are going to visit, in some cases live, and experience first-hand the consequences of these assistance programs. Because we can serve as a permanent bridge between the United States and the countries of the CEE and NIS.

But the issue is not just increased effectiveness and efficiency in our foreign assistance programs. There is an even more important reason for immediately engaging both U.S. government departments and agencies and private sector organizations with long-term interests in the region.

What is at stake here? **Nothing less than the national security interests of the United States!** In this century, the United States was called upon to fight two world wars and a 45-year cold war -- conflicts which emanated from the heart of Europe -- in the furtherance of vital U.S. geo-political interests. There is no greater U.S. interest than the dismantlement of the Soviet/Warsaw Pact strategic and conventional threat to the United States and our European allies. The institutionalization of democracy and market economies in Central and East Europe is the best means of guaranteeing that there will be no return to the days of the cold war nor any future European conflicts which will entangle the United States. The achievement of that objective, however, requires the continued engagement, support, and assistance of the United States and the West.

An investment in peace, stability, and democracy in Central and East Europe serves U.S. long-term national interests in another way. After investing tens of billions of dollars in the cold war, the investment now required in **effectively run** U.S. assistance programs in the region pales by comparison. This investment in democracy building today will pay dividends through long-term security and reduced military expenditures for the United States.

In assuming the management of U.S. assistance to the region, USAID and its contractors unambiguously proclaimed that they will be in Central and Eastern Europe only for the short run. From the very start, these agencies and their Congressional supporters have promoted a shut-down schedule through which they will "graduate" individual countries from U.S. assistance as quickly as possible. (To date, USAID has failed to provide a rigorous, comparative, objective analysis and explanation for its "graduation" timetable and standards, an issue itself worthy of separate hearings.) This approach is incompatible with U.S. long-term strategic interests in the region.

The end of communism in the CEE/NIS and the tearing down of the Berlin Wall have opened up a whole new era for American foreign relations for both the public and private sectors. As President Clinton said in Berlin last year, "Everything is possible."

Many of these new opportunities are exciting and wonderful. American businessmen are exploring all sorts of exciting new investment and trade opportunities. Families and friends are meeting again for the first time after half a century. Colleges and museums are exploring and finding whole new worlds of science and long lost worlds of culture.

Other conditions are tragic. The environmental community is groping with catastrophes it could never have imagined. Grass-roots democracy building in the area of

public administration cries out for assistance. Human rights and welfare organizations are just beginning to comprehend the human devastation of decades of intolerance and inhumanity.

Whether it is building on new opportunities or trying to solve human or environmental disasters, U.S. public and private agencies have long-term strategic interests in the region.

In this context, the "bottom line" turns out to be actually very simple -- **The U.S. has long-term strategic interests and needs in this region. Thus, it is vitally important that all short-term U.S. assistance programs be designed and implemented in such a fashion so as to further these strategic interests and needs.**

The issue before this Commission, before this Congress, and before the entire country is **not** FY 1996 funding levels for the CEE/NIS. The issue is: What should U.S. relations with the CEE/NIS countries look like **15 and 30 years from now**, and what must we do **today** to make this happen?

The current process of managing U.S. assistance to the region is fatally incompatible to this goal. **A U.S. agency, with an emphatic short-term interest in the region, is managing billions of dollars which will form the bedrock of long-term U.S. relations with the countries of the region well into the next century.** This is a guaranteed formula for continuing catastrophe.

Thus, we ask that the Commission be fully engaged in the "zero-based analysis" of the management of U.S. assistance. We welcome the efforts of the Secretary of State, the Chairman of the Senate Foreign Relations Committee, and others to wholly re-invent the foreign assistance bureaucracy. Our concern, however, focuses less on the organizational structure of that bureaucracy and more on the delivery of effective and efficient assistance to the nations of Central and East Europe. The recommendations of the Coalition, provided in the addendum to this testimony, could serve as the basis of any reform effort. The reinvention will be judged by its results.

In summation, we urge the Commission to focus, for the short term, on immediate remedies the Coalition has recommended for the USAID contracting process, all of which can be implemented administratively with no new legislation. For the long-run, we ask that the Commission and the relevant authorizing and appropriating committees consult closely with the member organizations of our Coalition in the process of re-inventing foreign assistance.

I thank the committee again for allowing the Central and East European Coalition to be represented this morning and am pleased to answer your questions.

# CENTRAL AND EAST EUROPEAN COALITION

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February 13, 1995

**FURTHER INFORMATION:**  
Eugene Iwanciw (202-347-8629)

## **STATEMENT ON THE ADMINISTRATION'S FY 1996 FOREIGN ASSISTANCE BUDGET**

The Central and East European Coalition strongly believes that the long-term national security and budget interests of the United States require a stronger commitment to the transition of Central and East European countries to full democratic and free market nations than is evident from the Administration's budget proposals. We support increased funding for the Freedom Support Act (FSA) and Support for East European Democracy (SEED) programs and urge that the assistance focus on those countries which have demonstrated progress in the establishment of democratic institutions and market reforms.

The Central and East European Coalition believes that peace, stability, and democracy throughout Europe serve the national security interests of the United States. In this century, the United States was called upon to fight two world wars and a 45-year cold war -- conflicts which emanated from the heart of Europe -- in the furtherance of those vital geo-political interests. The institutionalization of democracy and market economies in Central and East Europe is the best means of guaranteeing that there will be no future European conflicts which will entangle the United States. We believe that with the collapse of communism and the Soviet Union, the objectives of peace, stability, and democracy in Europe are achievable. For those objectives to be achieved, however, requires the continued engagement, support, and assistance of the United States and the West.

Since the signing of the Camp David Accords, the United States has wisely supported the peace process in the Middle East. That long-term commitment is now paying dividends with increased stability throughout that region of the world. Similarly, the strengthening of democracy and market economies in the countries of Central and East Europe will require a long-term commitment by the United States. Forty-five to seventy-five years of communist oppression and tyranny cannot be eradicated overnight.

At a time when support for the emerging democracies, to insure success at this critical stage of their transition from totalitarianism to pluralism, is needed the most, the United States is reducing both its direct and indirect support for that effort. The reduction of funding for the Freedom Support Act from previous year levels is one example. The cutback in resources for objective information dissemination in the region through a viable Voice of America and Radio Free Europe/Radio Liberty as well as proposed cuts in funding of the National Endowment for Democracy are others.

The United States spent tens of billions of dollars to win the Cold War. It would be tragic were the United States to lose the peace through short-sighted policies. An investment in democracy building today will pay dividends through long-term security and reduced military expenditures for the United States.

# CENTRAL AND EAST EUROPEAN COALITION

## FOREIGN ASSISTANCE AGENDA

The Coalition seeks to promote the restructuring of foreign aid programs to better utilize Region Specific Organizations. RSO's, many of which are American ethnic organizations, initiated self-financed programs to help institutionalize democracy and free market principles in Central and Eastern Europe. These non-governmental organizations maintain a long-term commitment and have an intimate knowledge of the countries and/or region. U.S. assistance, funnelled through these organizations, would provide greater dividends than under current arrangements.

## REGION SPECIFIC ORGANIZATIONS ARE IMPORTANT TO U.S. DEVELOPMENT PROGRAMS IN CENTRAL AND EAST EUROPEAN NATIONS

**Summary:** Region specific organizations (RSO) are American non-governmental organizations (NGO) whose scope of work is limited and specific to one country or particular groups of countries in Central and Eastern Europe, including the new independent states. Many of these RSO's are U.S. ethnic organizations with strong, historic ties to the former Soviet bloc nations.

RSO's are engaged in a range of projects to strengthen U.S. relations with the countries in this region such as: providing humanitarian assistance; supporting democratic, free markets, and pluralistic reforms; supporting human rights; and promoting policies and programs to foster regional cooperation and peaceful resolution of conflicts.

RSO's have mobilized millions of dollars of private resources and will continue to do so long after U.S. Government funding is completed. The structure of government assistance programs has failed to take advantage of or to support this private sector effort. Government contracting procedures, especially at AID, must be reformed to include RSO's in development work in Central and East European countries.

**Background:** In initiating development programs for Central and East European countries, the U.S. Government has relied heavily on a traditional list of contractors, including both consulting and accounting firms and non-profits, almost all of which had long-standing working relationships with government agencies. While these organizations offer the U.S. Government immediate resource pools, and administrative structures with which government contracting offices are comfortable, they bring scant knowledge of specific developmental needs, geographic or cultural expertise, political and economic insight, or a long term commitment to the region. In fact, many of these contractors rely on RSO's for needed advice, technical expertise, cultural sensitivity, and manpower resources. However, RSO's are often ineligible for U.S. assistance to initiate their own programs.

RSO's, because of their regional commitment, offer a much higher "bang-for-buck" ratio in being able to implement top quality programs, specifically tailored to each country's needs, at a lower cost than generic contractors, whose interest in the region will cease upon suspension of U.S. government funding. To date, U.S. Government program design and contracting practices have failed to provide maximum assistance for every scarce dollar committed to the region.

**Recommendations:** The U.S. Government, through its implementing agencies, should reform its procedures to allow RSO's to participate in foreign aid programs. Specifically, such reforms include: the use of RSO experts in determining development priorities; open competition for all government contracts; tailoring requests for proposals to specific country needs (as opposed to generic regional needs); and a requirement for the contracting agent to indicate how work will continue after U.S. Government funding ends.

# CENTRAL AND EAST EUROPEAN COALITION

## RECOMMENDATIONS FOR REFORM OF USAID/USIA PROGRAMS IN CEE AND NIS NATIONS

The Central and East European Coalition is pleased to submit the following set of recommendations to improve the efficacy of programs funded by the United States and administered by USAID or USIA to the nations of Central and East Europe (CEE) and the New Independent States (NIS):

1. **Region Wide Contracts:** USAID and other government agencies grant many contracts on a region wide basis, i.e. throughout the entire Central and East European (CEE) region served by the SEED program or the entire Newly Independent States (NIS) served by the FSA program. This process eliminates region specific organizations (RSOs), those American non-governmental organizations such as the Polish American Congress, Ukrainian National Association, U.S.-Baltic Foundation, etc., whose scope of work is limited to one country or specific groups of countries in CEE/NIS. Also, region-wide grants often fail to address the specific needs of countries such as their political, economic, and cultural circumstances, their stage of political and/or economic development, and their nation's priorities. The result is a "one-size-fits-all" program for as many as twelve nations or administered through a series of contracts and subcontracts which multiply overhead expenses and add layers of bureaucracy to the program.

### **Recommendations:**

- \* Grants should be awarded for country specific programs or, in cases of groupings of small countries, for programs for limited regions, i.e. Baltic States, former Yugoslavia.
- \* Program awards for countries should be competed on a country-by-country basis and not by region.
- \* Any government agency which issues a RFP for a region-wide program in the CEE or NIS must provide justification based on the merits of a region-wide program and not related to administrative convenience.

2. **Grant Competition:** Many contracts in the CEE/NIS are being awarded without a competitive process. This process prevent RSOs from competing for many of the grants.

### **Recommendations:**

- \* Beginning in FY95, all U.S. assistance programs for CEE/NIS, with the exception of emergency humanitarian assistance, must be open to competition



through RFPs and RFAs. Any non-competitive awards can only be awarded in consultation with the Senate and House appropriations committees.

- \* No grants awarded in previous years should be extended through amendments and/or extensions if additional government funding is involved.
- \* The USAID office for PVO's shall publish and disseminate a weekly list of RFP/RFAs issued by USAID and all other U.S. assistance agencies to any registered PVO which requests to be put on a special mailing list designed for this purpose.

3. **Long Term Commitment/Private Sector Support:** U.S. national interest demands that the U.S. establish long-term relations with the newly emerging democracies of CEE/NIS. The democratic and free market reform progress will take many decades, especially in the NIS and Baltic Nations. Thus, contractors managing U.S. assistance grants must have long-term commitments to these nations, including a strategy for continuing their work after U.S. government funding has ended. Types of alternative funding might include grants from private and corporate foundations, corporate funding, establishment of endowments, or a membership base providing private sector funding.

#### **Recommendations:**

- \* Beginning in FY95, all RFPs/RFAs for U.S. assistance programs must include questions inquiring as to the long-term commitment of the applicant institutions in supporting development programs in the countries for which the grant is to be awarded, as well as a brief description of sources of non-governmental funding for the project in the out years.
  - \* For NGOs/PVOs which can offer immediate assistance but whose mission does not include a long-term commitment to CEE/NIS, programs should be designed to gradually transfer the functions during the period of US Government funding, to such organizations and institutions which have both a long-term commitment and a private funding strategy.
  - \* Applicants for development programs be required to identify local groups or organizations that the U.S. based PVO will partner or work with. The proposals should require seed money for and training of indigenous NGOs/PVOs to assume the responsibility for the program over time.
4. **Requirement for Local Contributions:** Currently U.S. and other western assistance programs do not always require the recipient nation or local program beneficiaries to contribute either financially or in-kind to the success of the project. Thus programs are too often handed to the recipients on "a silver platter," to the extent that some of the beneficiaries actually earn a substantial income from the program. Such benefits include overly generous travel expenses and per-diem. Also U.S. contractors are paying very high rates for office space and lodging in CEE/NIS,

which eat up a huge portion of the grant. Finally, some U.S. contractors are paying exorbitant wages and fees for local consultants and staff, many times higher than the prevailing local salaries for persons of specified skills, which causes tremendous "wage inflation" and makes it increasingly difficult for small NGO's working in the region to be competitive in hiring qualified local staff.

#### **Recommendations:**

- \* Each RFP/RFA should require that the grantees identify local (host government or organization) financial or in-kind contributions in support of the specific project (office space, vehicles, housing, local support staff, etc.). Humanitarian or emergency programs may be exempted from this requirement.
- \* U.S. Government agencies should require that salaries and fees paid for local staff and consultants be in line with prevailing local salaries based on the salaries paid by the U.S. Embassy for comparable work.

5. **Public Disclosure of Contractors and Projects:** Unlike the National Endowment for Democracy (NED) and private foundations, USAID has not provided public reports on their grants, i.e. which contractors have received funding, the level of funding for specific contracts, how the contract was awarded (through a competitive bid or a closed process), or project design and accomplishments.

#### **Recommendation:**

- \* USAID, USIA, and other grant issuing agencies should publish a quarterly reports of grants awarded by country, succinctly detailing the recipient, amount, and purpose/goal of each grant. USAID should also keep a file of brief (2-3 page) executive summaries, available by request from the public, of specific project designs, purposes, goals, and timetables. Each report should provide a summary of the "per unit cost" (including all costs, both overhead and direct program) of the program (e.g. for exchange, U.S. volunteer, and internship programs, the total cost per participant of the program; for technical assistance and consulting, the hourly or daily rate).
  - \* All federally funded concept papers and proposals must be classified public information and, upon request, access should be granted to them.
6. **\$60,000 USIA Probationary Cap:** The USIA has placed a \$60,000 probationary cap on grants to organizations with less than a four year track record in managing international exchange programs. This arbitrary cap discriminates against professional, effective organizations (many of which were providing support for the development of democratic and free market institutions in CEE/NIS nations even before the democratic revolutions in 1991) which are competent, qualified, and have long-term commitments to support reforms in this region. The current process favors large generic, traditional recipients who manage programs world-wide.

### **Recommendation:**

- \* USIA should immediately modify its \$60,000 probationary cap and establish more flexible guidelines for weeding out unqualified applicants and should include competence and uniqueness as criteria. Changes in the policy should include:
  1. lifting of the probation for NGO/PVO's which are registered with USAID;
  2. lifting of the probation for organizations which have successfully managed USIA USIA or USAID grants; and
  3. reducing the probationary period from 4 years to 1 year.
- \* In defining a track record in managing international exchange programs, USIA should include the self-financed work of organizations, not just U.S. government financed programs.

7. **Operating Grants to Strengthen Overseas Operations of PVO's:** Until recently, USAID's PVO office had annual competitions for U.S. PVO/NGO's working overseas for grants to strengthen their overseas operations (approximately \$1,000,000 for ten grants).

### **Recommendation:**

- \* USAID should bring back this program and open the competition to PVOs/NGOs who have a long-term commitment to development in CEE/NIS nations.
- \* USAID should re-establish its program to provide seed money for field offices to organizations which have been or are being established to support long-term privately funded programs.

8. **Country or Region Specific Knowledge:** Most of the organizations being awarded grants for work in Central and Eastern Europe have little or no experience in the region and often little or no knowledge of the political, economic, social, and cultural conditions in the target countries. They also often lack people with the linguistic ability for the specific countries. This has often led to the development of programs which are, at best, inappropriate or, at worst, counterproductive to the interests of the United States.

### **Recommendations:**

- \* USAID, USIA, and other grant issuing agencies should require, (except for emergency or humanitarian aid projects) as part of the application process, a demonstration by the applicant of a detailed knowledge of the target nation.

- \* USAID, USIA, and other grant issuing agencies should encourage organizations applying for grants in Central and Eastern Europe to team up with RSOs which have experience working within the target nation.

9. **History of Support for Democracy:** In some case, organizations which worked closely with the Soviet government during the period of the Soviet Union are being awarded grants to promote democracy and the development of NGOs in the CEE/NIS. This has caused a reaction among some elected officials, particularly former dissidents, in the target countries since the organizations now receiving U.S. Government grants were the same organizations lending legitimacy to the former regime.

**Recommendation:**

- \* USAID, USIA, and other grant issuing agencies should require, as part of the application process, a chronology of all contacts with any CEE/NIS governmental and/or nongovernmental entities and a brief outline of its history of promoting democracy within CEE/NIS during the past ten years.

10. **RSO Outreach:** RSOs are engaged in a range of projects to strengthen U.S. relations with the countries in the CEE/NIS such as: providing humanitarian assistance; supporting democratic, free markets, and pluralistic reforms; supporting human rights; and promoting policies and programs to foster regional cooperation and peaceful resolution of conflicts. RSO's have mobilized millions of dollars of private resources and will continue to do so long after U.S. Government funding is completed due to their long-term commitment to the countries of this region. It is in the long-term interests of the U.S. Government to strengthen the abilities of RSOs in the delivery of assistance.

**Recommendation:**

- \* USAID, USIA, and other grant issuing agencies should be required to initiate outreach programs to RSOs working in the CEE/NIS and provide them assistance with the application process.
- \* USAID should be required to establish an ombudsman whose mission will be to work with RSOs and other organizations with a long-term commitment to CEE/NIS nations.

11. **Ethics and Conflict of Interest:** There have been reports suggesting a high degree of socializing between USAID program and contract officers and USAID contractors and grantees in Eastern Europe. Examples include excessive and lavish meals, theater and opera tickets, organizing of "retreats" and "seminars" in resorts, and extensive trans-Atlantic and intra-European trips. These activities may violate conflict-of-interest or other ethics regulations.

**Recommendation:**

- \* USAID's ethnics office should initiate an aggressive, pro-active program to educate and train USAID staff on correct ethics procedures to avoid conflict of interests violations in their dealings with contractors and grantees.

12. **Program Design:** USAID routinely recruits consultants, in a non-competitive manner, for program designs. It is not known on what basis these consultants are chosen or the degree of CEE/NIS experience these consultants possess. It is also not known whether the consultants used in the design process are allowed to compete for the programs which are designed through their work.

**Recommendations:**

- \* USAID should establish a formal, public procedure for the recruitment of consultants for the design of programs for CEE/NIS nations and a statement as to whether those involved in the designing of the program will be allowed to compete for the grant. USAID's Ethics Office should review these procedure.
- \* USAID should conduct a pro-active campaign to involve RSOs with extensive experience in the target nations in the program design stage.

13. **USAID-funded Products:** Currently, any programs or products developed by USAID-funded programs become the proprietary product of the grantee. This results in a great degree of waste since similar programs or products are being redeveloped by different grantees rather than building on the knowledge and/or success already achieved.

**Recommendation:**

- \* USAID, USIA, and other grant issuing agencies should provide in any contracts for CEE/NIS nations that the programs and products developed as a result of the grant become the proprietary product of the U.S. Government and can be shared, at the discretion of the appropriate government agency, with other government grantees.

14. **Streamlining:** Currently, RFPs and contracts issued by USAID, USIA, and other grant issuing agencies involve complicated procedures and extensive paperwork. This prevents smaller, competent organizations which maintain a low-overhead from competing for the grants. It virtually requires that organizations maintain large staffs which is ultimately funded by the grants.

**Recommendation:**

- \* USAID, USIA, and other grant issuing agencies should review their procedures for the issuance of RFPs and contracts in an effort to simplify and streamline the procedures and paperwork.

- \* USAID, USIA, and other grant issuing agencies should initiate a program to assist RSOs specializing in CEE/NIS nations including the convening of workshops on a periodic basis.

15. **Language:** As part of its russification effort, the Soviet Union imposed the Russian language on the nations of Central and Eastern Europe, particularly on the former republics of the Soviet Union. Upon independence, many of these nations enacted laws establishing their native languages as state languages. While the U.S. Government conducts relations with these nations in their native languages, even in the absence of these laws, USAID and USIA grantees often conduct programs solely or predominately in Russian. The U.S. is thus often perceived as a continuing the Soviet policy of russification.

**Recommendation:**

- \* USAID, USIA, and other grant issuing agencies require, as part of their contracts with grantees, that programs within a given country be conducted in the state language of that nation or, in the absence of a law stipulating the state language, the language used predominately in United States diplomatic relations with that nation.



## CSCE PRESENTATION

February 17, 1995  
John D. Sullivan

### I. INTRODUCTION

The work of the Center for International Private Enterprise draws on the experience base of our parent organization, the US Chamber of Commerce and especially our member companies. Over the last eleven years, we've been supported by the National Endowment for Democracy, more recently by USAID, and by private foundations like the Pew Charitable Trusts. All told, we've been directly involved with over 300 projects in some 50 countries including most of Central and Eastern Europe, Ukraine, Russia, and Belorussia.

As many of you probably know, the US Chamber has been involved with Central and Eastern Europe for over thirty years through a series of bilateral economic councils. That relationship was not always a happy one since it tended to mirror the overall relationship between the US and the various countries in the region. The involvement with the former Soviet Union was less direct though a number of our major member companies were involved in the region.

CIPE has only been involved in Central and Eastern Europe since 1989 and in Russia and the NIS region since 1991. We waited until we saw a commitment to a real change in the state of the system until we began working through the Center. (More on this point below).

What I thought would be useful today would be to comment on our overall strategy and the lessons we've learned from the sixty or so projects that we've been involved with over the last six years in these two regions. In particular, I'll focus on some of the lessons we've learned in the area of strategy and then some of the basic management lessons coming out of this experience.

We've passed out a portfolio which describes most of these projects for your review. As you'll see, for the most part CIPE forms partnerships with local private sector groups to



advocate market reform, build institutions, promote entrepreneurship, and related activities. Most of our partners are business groups, either associations of entrepreneurs, foundations, public policy research institutes, or chambers of commerce. In fact, though, we've not done many projects with the chambers in the region since they tend to be holdover organizations closely connected to the state institutions. Poland and a few others are exceptions.

Let me add one caveat given that the purpose of today's meeting is to focus on the goals and accomplishments of the foreign assistance effort in the region. The programs that we're involved with are what might be loosely called grass-roots projects with private sector groups or what those in government tend to call non-governmental organizations. This is a relatively small percentage of the US government's overall foreign assistance portfolio -- though we think it is an absolutely crucial percentage. Some of the points that come out of our experiences could be extrapolated to other areas, including government-to-government efforts, though I would urge caution in making that leap.

## II. BACKGROUND CONDITIONS IN THE REGION

By way of background, let me just refer to a couple of points regarding these two regions which are generally well known but tend to get lost in the shuffle.

First, there has been a tremendous amount of progress in Central Europe, especially in Poland, the Baltics, and the Czech Republic, and to a fair degree in Hungary. Although less has been done in the Southern Tier countries, many have still made steady progress in adjusting to new realities. I'm not going to go into a comparative review of each country. Let me instead refer you to the magazine we've handed out *Economic Reform Today*. As you'll see, the current issue contains reports on many of these Central and Eastern European Countries compiled by independent public policy research institutes like the Gdansk Institute for Market Economy in Poland.

Let me make two points about this material, though. First, in judging the amount of progress or lack thereof, it's vital to keep in mind that **there is no benchmark or yardstick or accepted standards of any kind** against which to measure what's been accomplished. To me it seems that those who were very optimistic about the pace and ease of reform in 1989 are disappointed today while those that were pessimists earlier are today quite pleasantly surprised.

A second point that can be kept in mind is that although there are no accepted standards, there are some indicators and one of these is the degree to which the countries have attracted **foreign direct investment** and the degree to which



they continue to do so. On this ground, indicators show that real and tangible progress has been made since 1989 in large parts of Central Europe, that much remains to be done in the Southern Tier, and that there is a lot of skepticism about possibilities in Russia and the NIS countries.

- American Chambers in the Region where none had been before. Not surprisingly, the last to be organized is the one in Russia which is still not an accredited AmCham by US Chamber standards though that is probably close.

Let me also say that there has been one other major change in the region as a whole since 1989 and that is in the nature of US interests.

- \* Starkly put, the old issues of military security have changed fundamentally.
- \* Simultaneously, the two regions' integration into the world trading system have raised a host of issues that have not been fully addressed including

- US investments
- Flow of investment funds
- Disruptions in the flow of commodities including oil, aluminum, and others
- Economic crime

We also need to explicitly recognize at least one major success that has taken place in Central and Eastern Europe. That is:

**democracy and market economics are generally accepted as the preferred way of organizing society.**

I would also say that there is a growing understanding of what these values mean both in the opinion leader groups and in the society as a whole. This is not to say that people are content with their governments since, in many cases they clearly are not. It is to say that the basic values have triumphed over a variety of other values including communism and state socialism.

Now I don't think that the US should crow like the Rooster that claims credit for brining up the dawn, but a lot of groups like ours have been involved in promoting these ideas over the years. In addition, a lot of US Government programs including Radio Free Europe and Radio Liberty have been right in the middle of the debate. Essentially, in Central and Eastern Europe at least, the war of ideas has been won.

However, it's our sense that the war of ideas isn't yet over in Russia and the NIS region. Although the old dogmas of Marxist-Leninist thought are gone and were probably only given lip service for a number of years, that doesn't equate to the acceptance of market economics and democracy in the region.

- A. Some simply don't have even the most basic idea what democracy is all about.
- B. Many if not most don't understand the basics of a market system or accept its most basic value -- property rights.
- C. In Russia and the NIS, as opposed to Central and Eastern Europe, relatively few have accepted or been able to operationalize the concept of **self-governing organizations** through which people can join together to accomplish limited objectives -- political parties, firms, trade unions, business associations, civic groups etc. are all developing much more slowly.

Because of the differences, the two regions are different and require very different strategies.

At a minimum, it has to be recognized that the capacity of private groups, governmental structures, and others to absorb assistance varies widely because of these differences. This is a fact that hasn't been appreciated and has led a lot of groups to end up badly disappointed with the results that they attained.

## II. Basic principles of CIPE's programs -- Strategy

- A. Drawn from American and overseas experience -- not in foreign aid per se but rather in trying to understand the forces that drive democratic development through economic, social, and political growth.

### B. KEY elements

- 1. Market based system with an Open and free political system, i.e. broad definition of democracy.

**Politics and economics can't be separated -- they're two faces of the same coin.**

- 2. Emphasis on key institutions such as property rights, free prices, regulatory environment

3. Policy regime that fosters economic health
4. Develop viable private sector groups that can play a key role in the advocacy process to craft policy reform recommendations and build public support for their adoption. Secondary role is to provide services and carry out other civil society type functions.

Could go on but I think you get the gist. Just as an aside, I'd like to say that these factors -- things like anti-trust law -- are not recent discoveries nor can they be taken for granted.

C. KEY STRATEGIC QUESTIONS:

1. Has the country made a firm commitment to a change in system?
2. Does the public and private leadership of the country understand what that commitment implies?

Obviously, the answers to those questions involve gray areas and a lot of judgment but they are key issues in the allocation of funds and how the strategy set for the country will unfurl.

III. What works and what doesn't work in the strategy area.

A. Develop tailor made strategies for each type of country or situation based on in-depth analysis

1. Stock of Institutions and organizations

-- is there a private sector, a banking system, a political party system, etc

The answers here may not be what you want to hear but its key to make such a realistic assessment to see what the **absorptive capacity** of the society actually is.

By the way, while a great deal of progress has been made in building the private sector and some progress in building effective party systems, the banking systems throughout the region remain a tremendous potential issue and one which there is little that can be done until a commitment is taken in each country to effect change.

2. Policy regime
3. Status and characteristics of business community
4. Educational levels
5. Political development

B. Avoid wishful thinking in an effort to be supportive.

1. Internal World Bank study on Tanzania
2. Just as an aside, it seems to me, speaking personally, that a lot of the debate over AID to Russia and the NIS really is based on some very unclear assumptions and lack of precision due to wishful thinking.

On the other hand, a lot of the criticism has been set against impossible standards. (This is essentially the point that Charlie Flickner makes in his article in *National Interest*. He also points out that there was no way many of these goals could have been achieved.)

C. Avoid oversimplifying and making assumptions

Let me give some examples of where this has occurred or can occur. Some of these, by the way, are things that we've managed to avoid only because of the long experience in the region. Other lessons we've had to learn as well.

1. What works in Latin America is not necessarily going to work in Eastern Europe or Africa or South Asia -- obvious but all too often ignored.

Sunday's *Washington Post* article.

2. Markets and business people don't simply emerge; they have to be developed.

Institutions and rules  
Informal sectors

3. Business is not a monolith.

Often, especially in Central Europe, the nature and interests of different groups varies widely.

One example of this is the way that the chambers of commerce are beginning to reorganize themselves. At the prodding of the West Europeans, especially the Germans, the national chambers, which were state organizations under Communist rule, are seeking to create mandatory membership organizations. That is they're seeking to pass laws requiring all firms to join the chamber, have the chamber be the business registry for the country, and provide other services normally provided by government.

Many of the private business associations are actively fighting against these measures while others are seeking to carve out new areas for themselves distinct from the national chamber movements.

Not all national chambers are trying to follow this model, but the point is that similar sounding names and functions often disguise a variety of different types of organization, some of which wouldn't be accepted in the Anglo-American version of a market based democracy.

4. The existence of private firms doesn't mean that a market system exists.

Property rights and clear rules are a much better indicator.

#### IV. MANAGEMENT

A. FIVE YEAR Review and annual reviews of key projects

-- portfolio approach that combines innovation and risk with some proven winners to sustain the program.

B. Target the assistance in small projects

1. Developing the private sector and private groups means that you can't simply give them continuing support or expand their budgets
2. No more than 35 to 50 % of existing budget unless there has been some exceptional circumstance.
3. Post-communist systems required some adaptation.

The wide disparities in exchange rate values and actual purchasing power means that one has to be more sensitive to the real *commitment* to a project rather than the easier task of just looking in dollar terms.

C. Matching Funds helps to focus the program better.

1. Our internal review found that of the unsuccessful projects, few had matching funds.
2. Individual effort  
Other cash support
3. Screening device

D. Project based programs are most important

1. Continuing or general organizational support usually doesn't seem to work because it removes the organization from its own supporters or members.
2. Project based support generates experience and marketable results.

E. Don't impose your priorities or insist on the type of project -- start from the organization's own priorities and goals as based on their members and/or supporters.

1. Must have local ownership for the project
2. Requires more work to match up individual projects with your own overall strategy.

V. **INTERNAL CONTRADICTION WITHIN MOST FOREIGN ASSISTANCE**

Now I realize that a lot of what I've laid out sounds like an ideal case. Part of the reason for that is the way the

procurement process works in bidding out and competing out projects. Let me give you some examples:

A. Most projects are created by the US Government's staff coming up with the idea and then bidding it out. Procurement regulations mandate this. However, this often results in some real problems:

1. Labor intensive work -- Type of skills

Staff/funding ratios are way off -- degree of management effort must be higher.

At least for the types of projects I've described which tend to be very labor intensive:

-- management plan or program of work  
-- budgeting it out

prior to the project identification.

Afterwards its a function of meeting key objectives and milestones, evaluating, and working out contingencies.

2. Often the requirements of procurement regulations and what works are in conflict.

\* Management approach should be based on objectives rather than just using the procurement codes to drive programs.

\* Form should follow function.

B. Scale of project

As can be seen from the types of projects I've described, most are in the range of \$75,000 to \$100,000 with some matching funds from the counterpart group.

This is the real absorptive capacity of most private groups in the Central and Eastern European region. In Russia, its difficult to find private groups that can handle projects of even that size.

-- A133 requirements  
-- Seperate bank accounts and accounting systems  
-- Management  
-- Personnel requirements

-- Skill base in areas like advocacy etc.

I'm sure that this will horrify the professional foreign assistance community who will rightly say that they have neither the time nor the capability to work on an indepth basis like this in all of the areas they are responsible for.

## V. OTHER LESSONS LEARNED IN THE CIPE PROGRAM

- A. Overall projects must address the key issues or factors in the environment, otherwise they are not developmental they are simply coping strategies.

### EXAMPLE      Microenterprise Programs

To really address the full range of issues related to developing microenterprises whether in Hungary or in Russia, a very complex range of issues have to be deal with on a priority basis:

1.    Access to finance -- reform of banks or creation of new financial intermediaries
2.    Policy change  
      Barriers to registration  
      Regulatory burdens -- labor law for example
3.    Human development  
  
      Entrepreneurial skills  
      Management -- business plans etc.
4.    Crime and corruption issues -- rule of law

A country strategy that doesn't address these issues is simply a coping strategy to help firms survive within a hostile environment. It won't do much in the long run.

- B. Business is not a monolith

1.    State firms
2.    Crony capitalists
3.    Informal sector
4.    Entrepreneurial sector
5.    Small business

Central Europe and Russia -- its vital to target the right group for a number of reasons.



When one is helping a chamber or trade association, you have to know who they are representing.

These same groups often form the basis for the political party structures in the country.

- C. The emerging think tanks and private sector associations are improving throughout Central and Eastern Europe but still need substantial assistance to meet their mandates as being key institutions to build and support a new market oriented democratic society.

CIPE's own in-house evaluation of many of the projects we've worked on point to the following areas for improvement:

- ◆ Research capabilities with respect to market economics concepts (performance and policies of micro and macro economies).
- ◆ Organizational structure and management (strategic and managerial planning).
- ◆ Financial Management (finance and budgeting, sources of non-dues income) and financial planning.
- ◆ Policy analyses and formulation of recommendations including the institutes' capabilities in public policy processes (i.e. tax policy analysis is very different from economic analysis of tax incidence).
- ◆ Education, dissemination, and advocacy capabilities including prior experience in publishing and holding conferences etc.

## VI. CLOSE

I'd like to close on a note of optimism and also to make an appeal for greater sophistication in targeting foreign assistance.

On the note of optimism, it does seem to us at CIPE that the groups we've been working with, many of whom were not in existence four or five years ago, are making great strides. They're beginning to:

- effect policy change toward the market
- produce talented people capable of assuming important positions in their countries
- reflect the true interests and nature of the emerging private sector, especially entrepreneurs, which is key to sustaining change.

-- despite the fact that many areas need improvement, these private groups do represent the development of exactly what one of the key aims of foreign assistance should be --- to foster the emergence of self-governing groups that can bring about economic and political reform.

Obviously, Poland, Hungary, the Baltics, and the Czech Republic are much further along, in part because they started out in the vanguard. However, new organizations are forming in the Southern Tier countries and the existing groups are showing positive signs as well.

In Ukraine, the development of a group of vibrant private sector organizations is, in fact, one of the few positive stories in the country and is a source of hope.

In most of the rest of the NIS, including Russia, the development of these organizations has not progressed nearly as far though there are signs that some may be showing progress. Paradoxically, the Russian Chamber of Commerce, one of the older organizations has made major strides to transform itself and take on a new role which has not happened in most other countries in the region. The other exception being the Polish Chamber.

The very last point I'd like to make follows from this concept of working with the emerging private groups. As we debate the future of foreign assistance and the issue of whether or not Russia or some other country merits help, lets begin to be a bit more strategic in our thinking. By this I mean:

- Differentiate between the government and the emerging private groups such that assistance to the private sector doesn't depend on or, in most cases, have to go through the government.
- Recognize that even though the government may not be making much progress in economic reform, democratic development, human rights, protection for intellectual property and other property rights, that its still in the US national interest to work with the emerging private groups.
  1. They represent an alternative to official thought
  2. They provide a window into the country which would not otherwise be available

3. They are an alternative government that may one day be in power. Providing assistance to these groups is one of way of building a different future.











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